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In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

JURISDICTIONAL STATEMENT

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ON APPEAL FROM THE SUPREME COURT
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JURISDICTIONAL STATEMENT

Moorman Manufacturing Company appeals from the final judgment of the Supreme Court of Iowa, Civil Appeal No. 2-60220, entered May 25, 1977, after order, entered June 27, 1977, denying Appellant's Petition for Rehearing. The judgment affirms assessment of additional Iowa income tax against Moorman. This Jurisdictional Statement is submitted to show that the Supreme Court of the United States has jurisdiction of the Appeal and that the questions presented are constitutionally substantial and of public importance.

The Appellees are G. D. Bair in his official capacity as Director of Revenue, State of Iowa and through him the State of Iowa.

OPINIONS BELOW

The opinion and order of the Iowa Director of Revenue dated December 17, 1974, is unreported. A copy is hereto attached as Appendix A. The Findings of Fact and Conclusions of Law of the District Court of the State of Iowa in and for Polk County, Equity No. CE 3-1595, filed December 17, 1976, the revision thereof filed January 7, 1977 (entitled Ruling on Joint Motion to Reconsider and Supplemental Findings), and that Court's Judgment and Decree are unreported. Copies are hereto attached as Appendix B. The opinion and judgment of the Supreme Court of Iowa entered May 25, 1977, is reported at 254 N.W. 2d 737 (1977). Copies of that opinion and the order denying rehearing entered June 27, 1977 are hereto attached as Appendix C. A copy of the Notice of Appeal filed in the Supreme Court of Iowa on August 4, 1977 is hereto attached as Appendix D.

JURISDICTION

Moorman challenged, in the District Court of the State of Iowa, an assessment of additional Iowa corporate income tax, §422.33(1)(b), Code of Iowa, "apportioning" Moorman's entire unitary income by the ratio of sales to Iowa customers to all sales, although all goods sold to Iowa customers were manufactured in Illinois.

For its fiscal years 1968 through 1972, Moorman apportioned its income for Iowa, Illinois (and other states) income tax purposes in accordance with the Uniform Division of Income for Tax Purposes Act, which provides a three-factor formula, equally weighted, of property, payroll and sales. Iowa has not adopted the Uniform Act.

The assessment was for the difference between the amount reported pursuant to the three-factor formula and the amount determined by the Director of Revenue on the sales-only formula.

Moorman appealed to the District Court which accepted Moorman's contentions that the statutory formula was unconstitutional on its face, on due process and commerce clause grounds, because of failure to recognize the contributions of capital and labor to the production of income and because of the double taxation resulting from the interplay of the Iowa and Illinois statutes, the latter employing the conventional three-factor formula. Moorman contended also that the application of the statute in this case made the statute void on those grounds and as a denial of equal protection. The District Court ruled against the equal protection claim and did not discuss application. The Director appealed, Moorman cross-appealed and the Supreme Court of Iowa ruled adversely to Moorman on all issues. Its judgment became final when it denied Moorman's petition for rehearing on June 27, 1977.

The jurisdiction of this Court to hear this appeal is conferred by Stat. 929, 28 USC 1257 (2), the issue being a state statute unconstitutional on its face and so applied as to burden unduly Moorman's interstate commerce, to deprive it of its property without due process of law and to deny it equal protection of the laws, contrary to Art. I, Sec. 8, Cl. 3 of the Constitution of the United States relating to interstate commerce and to the due process and equal protection guaranties of the Fourteenth Amendment thereto. The following cases sustain such jurisdiction: *Dahnke-Walker Milling Co.* v. *Bondurant*, 257 U.S. 282, 288-289 (1921); *Bantam Books Inc.* v. *Sullivan*, 372 U.S. 58 (1963); *Wheeling Steel Corp.* v. *Glander*, 337 U.S.

562 (1949); *Huffman* v. *Pursue, Ltd.*, 420 U.S. 592 (1975): "Moreover, where a final decision of a state court has sustained the validity of a state statute challenged on federal constitutional grounds, an appeal to this Court lies as a matter of right." (420 U.S. at 606).

QUESTIONS PRESENTED

Interstate Commerce, Due Process, Territorial Jurisdiction and Equal Protection

Whether the single-factor destination sales formula for the "apportionment" of net income, prescribed by the Iowa income tax statute, is invalid:

(a) as repugnant to the Commerce Clause of the Constitution;

(b) as repugnant to the Due Process Clause of the Fourteenth Amendment to the Constitution;

(c) as unconstitutionally extending the power of the State beyond its territorial jurisdiction;

(d) as repugnant to the Equal Protection Clause of the Fourteenth Amendment to the Constitution;

when the application of such formula results in the taxation by Iowa of 100% of the net income of a foreign corporation derived from that segment of its business consisting of the manufacture of products without Iowa and their sale to customers within Iowa, while a domestic corporation pays no Iowa income tax with respect to its exports, thus

(1) discriminating against interstate commerce by imposing upon it cumulative tax burdens (double taxation) to which local commerce is not subject;

(2) subjecting to Iowa tax an amount of income out of all reasonable proportion to the business actually done within Iowa;

(3) taxing extraterritorial values and assigning to Iowa values which belong to, and have been properly taxed by, another state (Illinois); and

(4) subsidizing exports and imposing a tariff on imports.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Art. I, Sec. 8, Cl. 3 of the Constitution of the United States and the Due Process and Equal Protection Clauses of the Fourteenth Amendment thereto are set forth in Appendix E-1, p. A99, *infra*.

The pertinent sections of the Code of Iowa, being Sections 422.33 and 422.35 contained in Volume II pages 1669 and 1670, Code of Iowa (1966) are set forth verbatim in Appendix E-2, pp. A100-A103, *infra*.

STATEMENT OF THE CASE

The operative facts were fully stipulated (R. Item 2, pp. 9-47), the sole issue on appeal being the constitutionality of the Iowa statute applied to those facts.

Moorman Manufacturing Company is an Illinois corporation headquartered in Quincy, Illinois. Its business is the manufacture of animal feeds which it sells to farmers and others in thirty states, including Iowa. During the years at issue, all goods sold to Iowa customers were manufactured in Illinois and no manufacturing was done in Iowa. Orders are solicited from Iowa customers by

a substantial force of resident salesmen and typically are filled from stocks in warehouses in Iowa to which they have been shipped from factories in Illinois.[1]

Appellant brought proceedings before the Iowa Director of Revenue for review of income tax deficiencies for the taxable years 1968 through 1972 assessed by him pursuant to the income tax section (Sec. 422.33) of the Code of Iowa. The Director affirmed the assessments. Moorman then appealed to the District Court, where there was trial *de novo*. The District Court found the statutory "apportionment" formula "facially unconstitutional" and struck most of the assessments (all that are involved in this Appeal). The Supreme Court of Iowa reversed the trial court and reinstated the assessments.

The assessments under Appeal are the differences between what Moorman paid, following the three-factor formula of the Uniform Division of Income for Tax Purposes Act, and the amounts asserted by the Director following the Iowa statutory single-factor formula of sales attributed to destination. The assessments tax 100% of Moorman's income from that segment of its business which consists of manufacturing goods in Illinois and selling them to customers in Iowa, taking no account of the contribution of capital and labor to the production of income.

The District Court found as *facts*: The Iowa single-factor formula taxed 100% of the income from each dollar of sales of Moorman's goods into Iowa, although 75% of payroll and 30% of capital are used in the manufacture of the goods (in Illinois) (App. B. p. A28, *infra*); the Iowa formula fails to reasonably apportion profits traceable

1. Moorman also made sales in Illinois which were delivered to Iowa. These were treated as Iowa sales under the statute in effect during the last year at issue and included in the controverted assessment. App. A, p. A2, *infra*.

to Illinois and taxes activities occurring in Illinois (App. B, p. A29, *infra*); the Iowa formula produces multiple taxation of the same income (App. B, p. A37, *infra*); Illinois taxed the relevant income by the three-factor formula (App. B, p. A33, *infra*); the Iowa formula taxed values beyond those which may be justly allocated to intrastate activity, and resulted in "gross overreaching" by the State (App. B, p. A33, *infra*); for 1968, the Iowa and Illinois formulae taken together taxed 141.76% of Moorman's income from its Iowa sales (App. B, p. A36, *infra*); Iowa is the only state attributing income to sales alone (App. B, p. A37, *infra*); the interplay of the Iowa and Illinois formulae would give unfair advantage to an Iowa manufacturer selling in Illinois in that only one-third of the relevant income would be taxed (App. B, p. A38, *infra*).

The District Court held, on the basis of those findings, that Iowa's single-factor formula violated the Commerce and Due Process provisions of the United States Constitution, and cancelled the assessments (App. B, pp. A40, A41, *infra*). Upon appeal, the Supreme Court of Iowa reversed.

The Supreme Court's opinion makes much of the point that an apportionment formula cannot be precise and hence approximation is all that is required (App. C, p. A78, *infra*). It asserts that a number of decisions of this Court approve single-factor formulae, without noting that none of them was anything like *this* single-factor formula (App. C, p. A72, *infra*). It quotes extensively from *General Motors Corporation* v. *District of Columbia*, 380 U.S. 553 (1965) but dismisses it as a statutory, rather than a constitutional, decision (App. C, p. A76, *infra*), incidentally pointing out that the Iowa statute contains no provision that income from interstate commerce shall be "deemed to" arise in both states (as the D.C. statute does), and says there is no due process requirement for such "deeming"

(App. C, p. A78, *infra*). It asserts that evidence does not establish either double taxation or taxation of extra-territorial values—ignoring the findings of fact (App. C, p. A80, *infra*). It denies that the assessments tax 100% of Moorman's income from Iowa sales because of statutory adjustments to the income *base*—thus relying upon an aspect of the tax law wholly irrelevant to apportionment, to conclude that Moorman had not shown that its income from Iowa sales had been taxed more than 100%, again ignoring the findings of fact (App. C, p. A82, *infra*).

The assessments were on a basis identical to that declared invalid in *General Motors Corporation* v. *District of Columbia, supra.* It was stipulated by the parties that if that basis is unconstitutional, the appropriate basis is the Uniform Act by which Moorman paid initially (R. Item 2, p. 19).

HOW THE FEDERAL QUESTIONS WERE RAISED IN THE PROCEEDINGS BELOW

The constitutional questions were presented and vigorously argued, both orally and in writing, at every opportunity and were considered by each of the three tribunals: the administrative proceeding, the District Court in the trial *de novo*, and the Iowa Supreme Court, as shown by their respective opinions (App. A, B, C, pp. A1-A96, *infra*). The questions raised, in each case contending invalidity under the pertinent provisions of the United States Constitution, of the statute both on its face and as applied, were: denial of equal protection; denial of due process; and burden on interstate commerce. In this appeal, while noting the equal protection point, reliance is principally upon the due process and commerce clauses.

The order of the Director of Revenue dated December 17, 1974, following statutory hearing, notes (App. A, p. A4, *infra*):

> The taxpayer contends that a single sales factor formula inherently violates the commerce and due process clauses of the United States Constitution. . .

The stipulation of February 20, 1976 (R. Item 2, p. 16) on which the case was tried *de novo* in the District Court, said:

> 33. The questions of law presented for determination in this case are as follows:
>
> • • •
>
> II. Constitutionality of the Single Sales Factor Formula.
>
> A. Whether section 422.33(1)(b), Code of Iowa, which requires that net income from the manufacture or sale of tangible personal property be apportioned to the State of Iowa for income tax purposes pursuant to the single sales factor formula is in violation of any of the following provisions of the Constitution of the United States:
>
> 1. The due process clause of Section 1 of the Fourteenth Amendment.
>
> 2. Article I, Section 8, Clause 3 (the commerce clause).
>
> 3. The equal protection clause of Section 1 of the Fourteenth Amendment.

The Stipulation followed the above issues as to unconstitutionality of the statute on its face with similar questions as to its unconstitutionality as applied (R. Item 2, p. 17).

In its brief to the Supreme Court of Iowa, Moorman stated:

> The District Court correctly determined that the single sales factor method . . . is facially unconstitutional as in violation of the due process clause of the Constitution of the United States . . . (R. Item 3, p. 7).
>
> The District Court correctly determined that the single sales factor method . . . is facially unconstitutional as in violation of the commerce clause of the Constitution of the United States . . . (R. Item 3, p. 13).
>
> The District Court erred in holding that the single sales factor method . . . does not violate the equal protection clause of the Constitution of the United States . . . (R. Item 3, p. 22).
>
> Moorman's brief similarly argued unconstitutionality of the statute as applied (R. Item 3, p. 30).

In answer to these contentions, the respective tribunals said: Director of Revenue (App. A, p. A6, *infra*):

> Moreover, because of the differences in the types of apportionment formulae and tax bases among the states, double taxation can and does result. And the use of formulae by other states where the taxpayer does business is not relevant . . . While it is true that Iowa's single factor formula does not give effect to the corporation's geographical distribution of property and payroll, there is no constitutional or statutory requirement that it must . . . The Director of Revenue finds that the Iowa single sales factor formula does not operate to subject taxpayer to taxation on a greater portion of his net income than is reasonably attributable to business or sources within this state.

District Court:

> . . . we conclude . . .
>
> (2) that Iowa Code Section 422.33(1)(b) does not violate the Equal Protection Clauses of either United States Constitution or Iowa Constitution;
>
> (3) that Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Due Process Clauses of both the United States Constitution and Iowa Constitution; and
>
> (4) that Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Commerce Clause, Article I, Section 8, Clause 3, of the United States Constitution because it
>
> (a) does not fairly apportion interstate business activity to intrastate tax values;
>
> (b) causes multiple taxation of corporate net income by more than one jurisdiction; and
>
> (c) provides local business with a direct commercial advantage not so enjoyed by interstate business.

(App. B, p. A40, *infra*)

Supreme Court of Iowa:

> . . . the statutory language on which the decision turned in *General Motors* . . . was the specific requirement that net income derived from a trade or business carried on within or without the District shall "be deemed to be income from sources within and without the District." It was the Court's interpretation of this statutory phrase—which has no analogue in the Iowa statute and can scarcely be found in the due process

clause—which was the fulcrum of the Court decision . . . we conclude that section 422.33(1)(b) calls for a method of allocation which is fairly calculated to assign to Iowa only that portion of the taxpayer's net income reasonably attributable to the trade or business done in Iowa (App. C, p. A78, *infra*) . . . [Because of deductions from gross income in arriving at taxable income]: Clearly, a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales (App. C, p. A82, *infra*).

* * *

We rely again on the principles recognized by the Supreme Court . . . in concluding use of the single-sales-factor formula provided by the statute does not violate the commerce clause of the United States Constitution (App. C, p. A82, *infra*).

* * *

No evidentiary justification is provided for a conclusion Moorman is somehow different from those corporations legitimately subject to the provisions of section 422.33(1)(b). In the absence of such evidence Moorman has not made out a sufficient case for overturning on constitutional grounds the application of the Iowa single-sales-factor formula to its net income (App. C, p. A87, *infra*).

THE QUESTIONS ARE SUBSTANTIAL AS A MATTER OF CONSTITUTIONAL LAW

This case is a true descendant of *General Motors Corporation* v. *District of Columbia*, 380 U.S. 553 (1965). The Supreme Court of Iowa has refused to heed the unmistakable logic of this Court and followed the path, which this

Court reversed, of the Court of Appeals for the District of Columbia Circuit. This case is not controlled by the *decision* in *General Motors*, which is statutory, but it *is* controlled by the *reasoning* therein, which is constitutional.

The facts, the local laws and the results are essentially the same. The difference is that in *General Motors* this Court could and did correct the interpretation of a Congressional statute, and hence did not ground its decision on constitutional considerations, whereas here the Iowa Supreme Court's interpretation of the Iowa statute is conclusive, and this Court is asked to apply the constitutional principles which *General Motors* expounded, but found unnecessary to apply, in that case.

The Iowa Court said that not all of Moorman's income derived from Iowa sales was taxed because deductions were allowed in computing taxable net income,[2] thus importing into an apportionment argument a wholly irrelevant discussion of base. The Supreme Court of Iowa apparently recognizes that multiple taxation of the income of interstate commerce, solely because it is interstate, unconstitutionally imposes upon interstate commerce cumulative burdens not borne by intrastate commerce.[3] Its sole justification for finding that the Iowa apportionment formula does not cause multiple taxation is that the Iowa Code, Section 422.35, allows certain deductions in arriving at net income subject to apportionment, such as a deduction of 50% of the taxpayer's federal income tax liability.[4] This approach ignores the fact, which should be obvious, that the definition of taxable income has no bearing on its apportionment. The definition of taxable income applies equally to both

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2. App. C, p. A82, *infra*.
3. App. C, p. A81, *infra*.
4. App. C, p. A82, *infra*.

domestic and foreign corporations and is controlling for this purpose. The Court is not at liberty to say "income" is something different from what the statute says.

This Court has recognized and reiterated that income is the product of capital or labor or both combined. *Stratton's Independence, Ltd.* v. *Howbert*, 231 U.S. 399 (1913); *Eisner* v. *Macomber*, 252 U.S. 189 (1920); and that income is earned by a series of transactions beginning with manufacture and ending with sales, *Underwood Typewriter Co.* v. *Chamberlain*, 254 U.S. 113, 120 (1920). Relying on those principles, it has approved formulae dividing income on the basis of location or utilization of property (*Underwood, supra; Bass, Ratcliff & Gretton* v. *State Tax Commission*, 266 U.S. 271 (1924)), and on the basis of the familiar three factors (*Butler Bros.* v. *McColgan*, 315 U.S. 501 (1942); *Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U.S. 450 (1959)). *General Motors* can itself be cited for each of those three propositions. The Court has never approved a single factor *sales* formula for the division of income.

As this Court said in *General Motors*:

> "The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves." (380 U.S. at 559).

The District Court found as a *fact* that substantial double taxation had actually occurred in this case; quoting the above from this Court it said: "Moorman finds its income taxed by both Iowa and Illinois exactly as the *General Motors* court described."[5]

In this case the total overlap is (as to 1968) 141.76%.[6] The principal reason it is not 167% is that Moorman has some property and payroll in Iowa, so that the income related thereto is not attributable to Illinois under that state's formula.

The Supreme Court of Iowa made no direct response to the findings of the district court, but repeated the oft-quoted language from *Wisconsin* v. *J.C. Penney*, 311 U.S. 435, 61 S. Ct. 246, 85 L. Ed. 267, 130 A.L.R. 1229 (1940):

> "The Constitution is not a formulary. It does not demand of states observance of rigid categories nor precision of technical phrasing in their exercise of the most basic power of government, that of taxation. For constitutional purposes the decisive issue turns on the operating incidence of a challenged tax. A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society... The simple, but controlling question is whether the state has given anything for which it can ask return."

The Iowa Court then went on to hold that the Iowa formula

> ". . . is fairly calculated to assign to Iowa only that portion of the taxpayer's net income reasonably at-

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5. App. B, p. A33, *infra*.
6. App. B, p. A36, *infra*.

tributable to the trade or business done in Iowa since the taxing power exerted by the statute bears fiscal relation to the protection, opportunities and benefits given by the state."[7]

There probably is no other passage in Supreme Court reports that is so often misapplied as Justice Frankfurter's felicitous phrases. There was in that case no quarrel with the apportionment formula. The issue was whether the "privilege dividend tax" was an additional income tax, and hence constitutional, or a tax on the "privilege" of paying dividends, which could not constitutionally be applied to Penney since all matters connected with dividends occurred in New York. The Wisconsin Supreme Court had said the tax was not an income tax. Justice Frankfurter and four other justices held that it was an income tax, and the quoted language tells why "practical operation" prevails over "technical phrasing." Four justices dissented on the ground it was not an income tax in practical operation. In that same opinion, Justice Frankfurter warned against relying on "Ambiguous intimations of general phrases in opinions torn from the significance of concrete circumstances. . ." The principal quotation was apt in the "concrete circumstances" of *Penney* but is meaningless in *Moorman*.

"The question" remains "simple", but it definitely is not "controlling" here. In the context of this case, in which the only issue is how much tax, not "whether", the Iowa court's language quoted above is an obvious non sequitur. It says the "apportionment" is fair merely because Moorman is taxable.

The district court recognized the distinction, quoting from *Norfolk & Western Railway Co.* v. *Missouri State*

7. App. C, p. A78, *infra*.

Tax Commission, 390 U.S. 317, 88 S. Ct. 995, 19 L. Ed. 2d 1201 (1968).

The Commerce Clause prohibits the imposition upon interstate commerce of such cumulative burdens to which intrastate business is not subject. *H. P. Hood & Sons, Inc.* v. *DuMond*, 336 U.S. 525, 538-539 (1949); *Western Live Stock* v. *Bureau of Revenue*, 303 U.S. 250, 255-256 (1938); *Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 157, 170 (1954); *J.D. Adams Mfg. Co.* v. *Storen*, 304 U.S. 307, 311-312 (1938); *Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U.S. 450, 458, 462-463 (1959).

As was recognized in *General Motors*, the sales factor does not *apportion* income; it merely identifies the income of the pertinent segment of the business. The purpose and effect of a destination sales factor is to subsidize exports and penalize imports. It is well to keep in mind that the constitutional inferences in *General Motors* were based upon, in addition to strong precedent, inescapable logic and fundamental principle concerning the sources of income, its geographical attribution and its measurement. Every bit of that base is equally present here and compels the same result.

In sustaining the tax in the face of the record and the findings, the Supreme Court of Iowa has placed itself in direct conflict with this Court's declaration that the *Underwood* and *Bass* decisions ". . . are not authority for the conclusion that, where a corporation manufactures in one State and sells in another, the net profits of the entire transaction, as a unitary enterprise, may be attributed, regardless of evidence, to either State." *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123, 132 (1931). This principle was reaffirmed in the *General Motors* decision: ". . . required is that the formula adopted for general ap-

plication take account of the geographical spread of the major dimensions of a business." 380 U.S. 553, 558, fn. 8.

The assessment, however, attempts to reach values not within the territorial jurisdiction of Iowa. The district court found as a fact that the income which Iowa taxed in its entirety was ". . . to a greatest degree attributable to Illinois plant and personnel inputs,"[8] and further found as a fact that the amount of income so assessed was out of all reasonable proportion to the business done in Iowa.[9] The Due Process Clause of the Fourteenth Amendment restrains States from taxing values not within their jurisdiction, *Wallace* v. *Hines*, 253 U.S. 66, 70 (1920), and prohibits the use of any apportionment or allocation which, either intrinsically or as applied in particular circumstances, taxes ". . . a percentage of income out of all appropriate proportion to the business transacted . . . in that State." *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123, 135 (1931).

Furthermore, even apart from the specific constitutional protection of "due process", a state may not reach transactions outside its territorial jurisdiction. *New York, Lake Erie & Western R.R. Co.* v. *Pennsylvania*, 153 U.S. 628, 646 (1894); *Miller Bros. Co.* v. *Maryland*, 347 U.S. 340, 342 (1954).

There is a strong pressure on local governments to defy the federal principle of a national common market. This is well illustrated by the shortsighted action of the Iowa Manufacturers Association in filing in the Iowa courts briefs *amicus* supporting the single-factor sales formula. It completely exempts them from Iowa tax on their ex-

8. App. B, p. A28, *infra*.

9. App. B, p. A33, *infra*.

ports, and heavily handicaps their out-of-state competitors in local markets. It is for such reasons that the Constitution makes the federal government, and this Court in particular, the arbiter of such matters.

In his order, the Director of Revenue noted: "Iowa is the only state requiring apportionment of income on the basis of a single factor formula. Most states allow corporations to file state income or franchise tax returns on the basis of some form of three factor formula, consisting of property, payroll and sales . . . Moreover, because of the difference in the types of apportionment formulae and tax bases among the states, double taxation can and does exist. And the use of formulae by other states where the taxpayer does business is not relevant.[10] Such a conclusion cannot be squared with this Court's opinion in *General Motors*.

While disagreeing with the District Court's analysis of and conclusion in the "equal protection" portion of the argument (he spoke of "corporations" as a class contrasted with other types of taxpayers, rather than "foreign corporations" as a class, contrasted with domestic corporations) we think Judge Critelli's opinion says about all there is to say on due process and interstate commerce. Insofar as it relates to those two issues, we adopt it.[11]

10. App. A, pp. A5, A6, *infra*.

11. App. B, pp. A17-A22, A25-A39, A40-A41, *infra*.

THE QUESTIONS ARE SUBSTANTIAL AS A MATTER OF PUBLIC IMPORTANCE

In *General Motors* v. *District of Columbia,* 380 U.S. 553, this Court noted that, while it seldom interfered with Court of Appeals interpretations of District statutes, it would do so when, as in that instance, there is ". . . an impact not confined to the Potomac's shores, but reaching far beyond" 380 U.S. at 556.

In Iowa more than fifty cases are awaiting the outcome of this one. And here again, the national impact is of far greater importance. Iowa is currently the only state out of 45 states (and the District of Columbia) imposing a corporate tax based on net income which is attempting to attribute to itself 100% of the income of foreign manufacturers selling to domestic customers; some others so disposed may have been discouraged by *General Motors.* If the Iowa statute is sustained the pressures mentioned above will surely induce others to follow suit, with the further consequences deleterious to the common market envisioned by this Court in *General Motors.*

A more subtle version is now appearing. States have begun to use sales and one other factor equally weighted, or to take all three factors and give sales double weight. There is an alarming trend: Florida, in 1971, adopted a new income tax weighting sales 50% and property and payroll 25% each. Wisconsin switched from equal weighting to a similar approach effective January 1, 1975, New York followed suit effective January 1, 1976 and Massachusetts did so effective January 1, 1977.

If the intent of the authors of the Constitution that this nation be an area of free trade is to be honored, this creeping return to protectionism must be contained. If

the decision of the Iowa Supreme Court is allowed to stand it will accelerate the politically-oriented tendency of state governments to adopt systems of taxation which "protect" home-based industry and raise barriers to out-of-state manufacturers, with the adverse results already recognized by this Court: "may tend to result in the unhealthy fragmentation of enterprise and an uneconomic pattern of plant location . . ." (*General Motors Corporation* v. *District of Columbia,* 380 U.S. at 560).

As the requirements of government, at all levels, grow, the pressures increase to shift the burden more and more to non-residents and non-voters, and the prime target is, of course, foreign corporations. When taxes, not so long ago, took only three percent of gross national product, the problem was less acute and less demanding; now when the take is more than ten times as much the need for strong reaffirmation of federalism is overwhelming.

CONCLUSION

The decision of this Court is needed to halt the effort of Iowa to shift its tax burden to foreigners and remove the temptation for other states to do likewise. The principles were well stated in *General Motors Corporation* v. *District of Columbia,* 380 U.S. 553, but because the Court expressly eschewed applying them in that decision as constitutional limitations on states the opportunity for the present overreaching was left technically open. It is now time to close it.

Following the decision in *Northwestern States Portland Cement Company* v. *Minnesota,* 358 U.S. 450 (1959), there was great clamor for protection of interstate com-

merce. In response, a group of state tax administrators urged their legislatures to organize the Multistate Tax Compact and Commission. The three-factor formula contained in the Uniform Division of Income for Tax Purposes Act (promulgated by the National Conference of Commissioners on Uniform State Laws and approved by the American Bar Association) has been strongly urged by the Commission for universal adoption.

In *General Motors* this Court said, "However, at times application of the District Code has an impact not confined to the Potomac's shores, but reaching far beyond. This is such a case. . . ." 380 U.S. at 556. Iowa has refused to adopt the Uniform Act and if the decision of its Supreme Court is allowed to stand, the *General Motors* decision will be rendered meaningless "beyond the shores of the Potomac."

It is submitted that the decision of the Iowa Supreme Court extends the taxing power of the State outside its territorial jurisdiction and beyond due process, interstate commerce and equal protection limitations imposed by the United States Constitution to the detriment of the national market. The constitutional violation here seems so obvious on the authority of *Stratton's Independence, Ltd.* v. *Howbert, Eisner* v. *Macomber, Underwood Typewriter Company* v. *Chamberlain, Bass, Ratcliff & Gretton Limited* v. *State Tax Commission, Hans Rees' Sons, Inc.* v. *North Carolina,* all *supra, Boston Stock Exchange* v. *State Tax Commission,* 429 U.S. 318 (1977)—and see also *General Motors Corporation* v. *District of Columbia*—that this ap-

peal deserves plenary consideration, with briefs on the merits and oral argument, for its resolution.

Respectfully submitted,

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APPENDIX

APPENDIX A

BEFORE THE STATE DEPARTMENT OF REVENUE
Lucas State Office Building
Des Moines, Iowa

IN THE MATTER OF THE CORPORATION INCOME TAX LIABILITY OF MOORMAN MANUFACTURING COMPANY, 1000 NORTH 30th STREET, QUINCY, ILLINOIS 62310

ORDER

This matter came on for hearing before the Director of Revenue on October 24, 1974. Present on behalf of the taxpayer were Walter R. Brown and John V. Donnelly, Attorneys. Present on behalf of the Director of Revenue were Ronald Amosson, Director, Income Tax Division, John Christensen, Auditor, Corporation Audit Section, and Harry M. Griger, Assistant Attorney General.

STATEMENT OF FACTS

The taxpayer, a corporation, is a manufacturer with its principal place of business at Quincy, Illinois. The taxpayer does no manufacturing in Iowa and its products which are delivered within Iowa are manufactured and sold within the State of Illinois. For the taxpayer's fiscal years ending March 31, 1968, March 31, 1969, March 31, 1970, March 31, 1971, and March 31, 1972, an assessment for additional corporation income tax was issued by the Department of Revenue against the taxpayer. The taxpayer protested this assessment and raised, prior to and at the hearing, four questions. Two of these questions

have been resolved between the Department and the taxpayer and are no longer in controversy. One of these questions related to the treatment of related expenses in §422.33(1)(a) of the Iowa Code. Taxpayer's computation of such expenses per its tax returns was accepted by the Department for the years in question. The second question involved the definition of "gross sales of the corporation within the state" in §422.33(1)(b) of the Code prior to amendment in §§37 and 38, Chapter 165, Acts of 64th General Assembly, First Session (1971). Prior to such amendment, the numerator of the statutory Iowa sales factor apportionment formula required that both the sale and delivery of the goods occur in Iowa. The amendment to this statute requires that only the delivery of the goods occur in Iowa in order that such sales be contained in the numerator of the formula. For the fiscal years ending March 31, 1968 through March 31, 1971, a portion of the taxpayer's sales which were included by the Department in the numerator of the single sales factor formula were made in Illinois with delivery in Iowa. Consequently, the assessment must be adjusted because such sales should have only been contained in the demoninator of the formula.

Therefore, the taxpayer presents two issues which the Director of Revenue must resolve. These are: (1). Whether the Department of Revenue may make additional income tax assessments within the six months limitation period set forth in §422.25(1) of the Iowa Code where such tax assessment is unrelated to any adjustment in the taxpayer's federal taxable income, and (2). Whether the Iowa single sales factor apportionment formula operated to subject the taxpayer to taxation on a greater portion of its net income than is reasonably attributable to taxpayer's business or sources within Iowa.

CONCLUSIONS OF LAW

The first issue involving the Department's authority to make an assessment of additional Iowa tax unrelated to adjustments in federal taxable income involves only the years ending March 31, 1968 and March 31, 1969. The formal tax assessment was issued on December 22, 1972. This assessment was issued within six months from the date of final disposition of controversy between the taxpayer and the Internal Revenue Service with respect to the years in question. However, the taxpayer contends that during this six months period, the Department was not authorized to assess Iowa tax on the ground of rejection of taxpayer's returns filed on a three factor formula basis and requirement of computation of Iowa income on the basis of the Iowa statutory single sales factor formula. The first sentence in §422.25(1) of the Iowa Code provides in relevant part:

> "1. As soon as practicable and in any event within three years after the return is filed the department shall examine it and determine the correct amount of tax, and the amount so determined by the department shall be the tax; . . ."

For the two fiscal years in question, this three year limitation period had expired prior to the issuance of the Department's assessment of December 22, 1972. During this period and in 1972, §422.25(1) provided in the second sentence thereof:

> *"Notwithstanding the periods of limitation for examination and determination heretofore specified,* the department shall have six months from the date of final disposition of any controversy between the taxpayer and the internal revenue service with respect to the particular tax year to make *the* examination and determination. (emphasis supplied).

The taxpayer contends that this above quoted second sentence of §422.25(1) of the Code only authorized the Department to make adjustments during the six months period which result from a change in federal taxable income and do not authorize the Department to make an adjustment and concomitant assessment due to a change from the three factor to single factor formula unrelated to any "controversy" with the Internal Revenue Service. However, taxpayer's contention ignores the plain meaning of this second sentence of §422.25(1) which clearly gives the Department additional time to make whatever adjustments, whether related to federal taxable income or not, necessary for a proper determination of taxpayer's Iowa income tax liability. To adopt taxpayer's contention is to read into this unambiguous statute words which are not there. Consequently, the Director concludes that the Department properly could, during the six months period, determine that the taxpayer improperly apportioned income to Iowa on the basis of a three factor formula and, thereby, assess taxpayer additional tax and interest on the basis of the Iowa single sales factor formula. The assessment of December 22, 1972, was timely made.

The second issue for the Director of Revenue to resolve on taxpayer's appeal is whether the taxpayer is entitled to file its income tax returns for all the fiscal years in question on the basis of an apportionment formula giving equal weight to sales, property and payroll or whether the Department can properly require the taxpayer to so file on the basis of the statutory single sales factor formula.

The taxpayer contends that a single sales factor formula inherently violates the commerce and due process clauses of the United States Constitution as applied to the states and, in the alternative, contends that it would be

an abuse of discretion by the Director of his authority contained in §422.33(2) of the Iowa Code to refuse the request of taxpayer, which does no manufacturing in Iowa, for permission to use a three factor formula.

A three factor formula consisting of property, payroll, and sales has been expressly held to be valid and constitutional by the United States Supreme Court. *Butler Brothers* v. *McColgan,* 1942, 315 U.S. 501, 62 S.Ct. 701, 86 L.Ed. 991; *General Motors Corporation* v. *District of Columbia,* 1965, 380 U.S. 553, 85 S.Ct. 1156, 14 L.Ed.2d 68. Iowa is the only state requiring apportionment of income on the basis of a single factor formula. Most states allow corporations to file state income or franchise tax returns on the basis of some form of three factor formula, consisting of property, payroll and sales. The formulae in effect in the states differ as to the tax bases to which such formulae apply. In the instant situation, the taxpayer would owe Iowa less tax on the basis of a three factor formula than on a single factor sales formula. Taxpayer, in support of its argument for use of a three factor formula, relies almost totally on *General Motors Corporation* v. *District of Columbia,* supra. While the Supreme Court criticized the use of a single factor sales formula, such criticism was within the context of a statute which did not authorize the use of such a formula, but seemed to require the use of a three factor formula. On the other hand, the following cases support the constitutionality of single factor apportionment formulae: *National Leather Co.* v. *Massachusetts,* 1928, 277 U.S. 413, 48 S.Ct. 534, 72 L.Ed. 935 (Single Property factor); *Underwood Typewriter Co.* v. *Chamberlain,* 1920, 254 U.S. 113, 41 S.Ct. 45, 65 L.Ed. 165 (Single Property factor); *Bass, Ratcliff & Gretton Ltd.* v. *State Tax Commission,* 1924, 266 U.S. 271, 45 S.Ct. 82, 69 L.Ed. 282 (Single assets factor); *Kent-Coffey Mfg. Co.* v. *Maxwell,* 1933, 204 N.C. 365, 168 S.E. 397,

90 A.L.R. 476, aff'd 291 U.S. 642, 78 L.Ed. 1040 (Single property factor); *Ford Motor Co.* v. *Beauchamp*, 1939, 308 U.S. 331, 60 S.Ct. 272, 84 L.Ed. 304 (Single gross receipts factor).

Moreover, because of the differences in the types of apportionment formulae and tax bases among the states, double taxation can and does result. And the use of formulae by other states where the taxpayer does business is not relevant. In *Commonwealth* v. *South Philadelphia Terminal, Inc.*, 1961, 404 Pa. 293, 171 A.2d 758, the Court stated at 171 A.2d 759:

> "The conclusion that the fairness of an allocation formula cannot be determined by consideration of or the effect of a different formula used by another state is most proper. The sole issue is whether Pennsylvania's formula justly allocates to itself a proper portion of the corporation's activities, regardless of the methods used by the other states."

This is also the issue under §422.33(2) of the Iowa Code. For all that appears, apportionment of the taxpayer's income by means of geographical distribution of sales of a unitary business is just as reasonable as the use of other formulae—a position taken by the State Board of Tax Review in *Phillips Petroleum Company* v. *Briggs*, Case No. 47, June 20, 1973. Apportionment formulae are simply approximations of the distribution of the sources of income of a unitary business or the social costs which such business generates. An iron rule of equality of taxation is neither possible nor attainable in this area. Merely because, under some circumstances, the use of a three-factor formula apportions less income to Iowa than the use of a single factor formula is not the test. While it is true that Iowa's single factor formula does not give effect to the

corporation's geographical distribution of property and payroll, there is no constitutional or statutory requirement that it must. "The Constitution is not a formulary". *Wisconsin* v. *J. C. Penney Co.*, 1940, 311 U.S. 435, 444, 61 S.Ct. 246, 85 L.Ed. 267.

The Director of Revenue finds that the Iowa single sales factor formula does not operate to subject taxpayer to taxation on a greater portion of his net income than is reasonably attributable to business or sources within this state. No showing has been made by the taxpayer that he is entitled to the use of a three factor formula over the single sales formula for the years in question. Taxpayer's request for permission to us a three factor formula to apportion income to Iowa is denied.

ORDER

It is hereby Ordered that the Income tax assessment be adjusted and revised for the years in question to be $236,890.00 tax plus interest as provided by law.

Done at Des Moines, Iowa, this 17th day of December, 1974.

/s/ G. D. Bair
G. D. Bair, Director, Iowa Department of Revenue

APPENDIX B

IN THE DISTRICT COURT OF THE STATE OF IOWA
In and for Polk County

EQUITY NO. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Defendant.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

(Filed December 17, 1976)

NOW on this 17 day of December, 1976, the above captioned cause coming on for trial before the undersigned on the 19th day of August, 1976, the plaintiff Moorman Manufacturing Company represented by Walter R. Brown and John V. Donnelly; the defendant G. D. Bair, as Director of Revenue for the State of Iowa, represented by Harry M. Griger, Assistant Attorney General; and appearing as amicus curiae by special leave of Court is the Iowa Manufacturers Association represented by James L. Rogers, John R. Phillips, and Russell L. Samson; the Court finds it has jurisdiction over the subject matter of this action and the parties hereto, and having heard legal arguments in this matter, having studied the stipulation of facts agreed between parties to be the evidence submitted, having carefully examined the extensive support provided for respective positions by briefs, after long and careful reflection, is now prepared to rule.

This action, putting squarely at issue the constitutionality of Iowa Code Section 422.33, finds its genesis in the defendant's December 17, 1974 order revising and adjusting Moorman's income tax assessment for that corporation's fiscal years of operation ending March 31, 1968 through March 31, 1972. The amount put in issue by that assessment, taxes and interest, totals $321,628.95. Moorman has taken appeal from the defendant's order affirming the revised and adjusted assessment by the provisions of Iowa Code Section 422.29 (1971) which cast this matter before the Court on a *de novo* basis. Because this cause has been submitted on an agreed stipulation of facts, no evidence beyond that in the stipulation was presented or is considered and as the parties to this action have requested by Paragraph 35 of said stipulation, this opinion merely makes findings of fact and conclusions of law but withholds the decretal or judgmental portion of this opinion upon which an appeal can immediately result.

PRELIMINARY FINDINGS OF FACT

The plaintiff, Moorman Manufacturing Company (hereinafter Moorman) is a corporation organized and existing under the laws of the State of Illinois and doing business in Iowa as well as several other states. For the period in question and currently, Moorman's principal source of income was generated by the manufacture and sale of more than eighty different products for feeding livestock and poultry with the greatest portion of those sales centered about the sale of mineral and protein supplements for livestock. Moorman's holdings are as extensive as they are scattered. It owns all of the outstanding stock of Quincy Soybean Co., Quincy, Illinois; the Moorman Manufacturing Company of California, Inc., San Gabriel, California; and Bell Grain and Milling, Inc., of Perris, California. Bell, in turn, owns all the outstand-

ing stock of Bell Milling Corporation of Escondido, California. Moorman's manufacturing facilities are located in five separate plants in three states: Quincy, Illinois; Alpha, Illinois; Comanche, Texas; Hereford, Texas, and Columbus, Nebraska. None of Moorman's manufacture occurs in Iowa. Moorman's products are principally sold directly to farmers and ranchers by its sales force of more than 2,500 salesmen, all paid on a commission basis, in more than thirty states of this country.

During the years in issue, March, 1968 through March, 1972, Moorman conducted a continuous solicitation and sales campaign to potential Iowa customers by its sales force of between 518 and 582 Iowa salesmen and warehousemen. Resulting sales were satisfied by delivery of its product from one to six warehouses in Iowa, located in Stanwood, Plainfield, Goldfield, Marcus, Atlantic, and Knoxville. The products sold in Iowa and delivered from one of the above distribution points were manufactured exclusively by Moorman's Illinois plants.

Due to its widely disbursed business activities Moorman pays income taxes to a number of states in addition to Iowa. It operates, for tax purposes, on a fiscal year basis ending March 31 of each year. Moorman's Iowa income tax returns for fiscal years ending March 31, 1968, 1969, 1970, 1971, and 1972 were all timely filed as required by statute and while the method of computation employed by it did not conform to the requirements of Iowa Code Section 422.33(1), the method used by Moorman was clearly disclosed on its returns for those years. Indeed, Exhibits 1 through 5 relating respectively to tax years March 31, 1968 through March 31, 1972, identify precisely the factors Moorman used to compute its Iowa taxes and cited as authority for so doing "General Motors Corp. v. D.C. U.S. Supreme Court Docket No. 352".

On December 22, 1972, D. G. Brigg's, defendant Bair's predecessor in office, issued an Income Tax Assessment Notice against Moorman relating to plaintiff's tax returns for its fiscal years of 1968 through 1972. That assessment found taxes and interest due from plaintiff respecting those fiscal years in the amount of $321,628.95, since Moorman had chosen to compute its taxes on the basis of a three factor formula and not the single factor sales formula of Iowa Code Section 422.33(1). Plaintiff's appeal from that assessment resulted in a hearing conducted before defendant on October 24, 1974. As mentioned above, it was defendant's December 17, 1974 order affirming the revised assessments which led to the appeal taken here.

The history of Moorman's tax intercourse with Iowa dates back to 1949 when it filed its first income tax return for fiscal year ending March 31, 1949. With approval of the Iowa State Tax Commission, Moorman, after allocating its interest, dividends, rents, and royalties, less expenses related thereto, apportioned the remainder of its net income to the State of Iowa on the ratio that its payroll, property, and sales within Iowa bore to its payroll, property, and sales everywhere through its operations in the United States, giving equal weight (.33) to each element in the ratio. This method of computation was followed for each year from 1949 to March 31, 1960. But at the direction of the State Tax Commission, Moorman computed its income tax obligation for the fiscal years of 1961 through and including 1965 by adherence to the single sales factor formula of Iowa Code Section 422.33(1). Beginning in its fiscal year of 1965, however, Moorman again applied the equally balanced three-factor—property-payroll-sales formula to its income thereafter. To this application of the three factor formula the State Tax Commission did not consent. It was the result of Moorman's

use for its fiscal years of 1968 through 1972 inclusive of the three factor formula that the December 22, 1972 notice of income tax assessment found additional amounts of tax due when recomputation conformed to the single sales factor tax formula of Iowa Code Section 422.33(1).

Based upon the facts submitted, more of which will be discussed in connection with each separately considered legal argument, the parties have presented several questions of law. Classified broadly and in the order in which such questions will be addressed below, we must determine (1) whether the statute of limitations in Iowa Code Section 422.25 defeats recovery by defendant of that portion of its revised assessment respecting Moorman's income for the fiscal years of 1968 and 1969; (2) whether the single sales factor formula of Iowa Code Section 422.33 is facially unconstitutional as in violation of the due process or equal protection clauses of the Fourteenth Amendment to the United States Constitution and the same provisions of the Iowa Constitution and in violation of the Commerce Clause of the Federal Constitution; (3) whether, depending upon the conclusions made concerning facial unconstitutionality, the single sales factor formula of our Code is unconstitutional as applied to Moorman as in violation of the same constitutional injunctions.

We turn to the problems posed by the statute of limitations in Iowa Code Section 422.25.

STATUTE OF LIMITATIONS

Iowa Code Section 422.25 reads, *inter alia*,

"*Computation of tax, interest, and penalties—limitation.*

"1. As soon as practicable and in any event within three years after the return is filed the department shall examine it and determine the correct amount of tax, and the amount so determined by the department shall be the tax; . . . Notwithstanding the periods of limitation for examination and determination heretofore specified, the department shall have six months from the date of final disposition of any controversy between the taxpayer and the internal revenue service with respect to the particular tax year to make the examination and determination."

Of the $321,628.95 the defendant assessed in arrearages by its Income Tax Assessment Notice of December 22, 1972, $62,073.77 is attributable to the defendant's revised assessment for Moorman's fiscal year ending March 31, 1968, and $59,272.03 represents the defendant's increased assessment for Moorman's tax year of 1969.

As noted above, Moorman timely filed its Iowa income tax returns for 1968 and 1969 indicating clearly, although not with defendant's consent, the apportionment formula it applied to income for those years.

Thus the three year statute of limitations in Section 422.25, unaffected by willful omissions or fraud considerations that would bring to bear either a six year or unlimited limitation period, began to run July 31, 1968 and July 31, 1969, and expired July 31, 1971, and July 31, 1972, respectively. Since the Notice of Income Tax Assessment bears the date December 22, 1972, the revised assessment respecting 1968 and 1969 would seem clearly to be uncollectible as beyond the limitation period. The catch is that Moorman's federal income tax returns were the subject of an audit by the United States Internal Revenue Service beginning in June, 1970 which called into question its returns for its fiscal years of 1968 and 1969. The audits were concluded by a written agreement between Moorman and the I.R.S. on or about October

8, 1973. The audit and agreement however resulted in no change which would affect the determination of how Moorman's net income arising from the sale of tangible personal property should be apportioned to the State of Iowa, whether by application of the statutory single sales factor apportionment method or by the three factor formula used by Moorman.

Although the audit and agreement respecting Moorman's income for those years made no difference in its income for Iowa's taxing purposes, by virtue of the federal inquiry the defendant contends the basic three year limitation period no longer applies because the revised assessment for 1968 and 1969 came well before "six months from the date of final disposition of any controversy between the taxpayer and internal revenue service with respect to the particular tax year. . . ." Section 422.25(1), The Code. Acknowledging that the audit produced no results upon which a change might follow in Iowa tax due, the defendant concedes that the audit by the I.R.S. is the only basis for its argument that the general three year limitation does not apply.

It is clear, as Moorman observes, that purpose of extending the primary three year limitation in Section 422.25 six months from the final disposition of any controversy between a taxpayer and the federal internal revenue service, is to allow the state to take advantage of the auditing efforts conducted under federal auspices.

While we believe the director would be remiss in his duties by failing to make "an examination and determination" of tax returns in the three year limitation period all the while awaiting possible institution of similar efforts by the Internal Revenue Service, the six months exception to the three year bar is neatly tailored to allow Iowa tax officials another opportunity in scrutinizing corporate

returns when federal examination of that taxpayer's returns results in adjustments which might present grounds for similar changes in Iowa tax liabilities.

Of course, the case here presents an added difficulty. If the federal audit discloses no information by which Iowa may make additional assessments, does the mere fact a federal audit took place leave the defendant a foothold for making a revised and adjusted assessment, otherwise barred by the limitation prohibition, and allowing him to recompute the corporate taxpayer's liability on the basis of taxing formula criteria different than the taxpayer disclosed in its returns?

We return to the statute for a more careful reading of the words our legislature chose to manifest its intent.

The duty of the department, to be accomplished "as soon as practicable and in any event within three years" from the filing of a corporate taxpayer's returns, is to 'examine' the returns and 'determine' the correct amount of tax. Section 422.25. Notwithstanding this general limitation, the department is given an additional six months which begins upon the resolution of a controversy existing between the taxpayer and Internal Revenue Service to 'examine and determine' the taxpayer's Iowa returns in light of the final disposition made between the taxpayer and Internal Revenue Service. During either the first three year period or a second six months extension, the scope of the department's inquiry respecting the taxpayer's returns is the same—the department must 'examine' and 'determine'.

Webster's Seventh New Collegiate Dictionary 288-9 (1965) defines the verb 'examine' to mean "to inspect closely; to test the condition of; to inquire into carefully. . . ." 'Determine', as a verb, is defined to include the

following actions: "to fix conclusively or authoritatively; to decide by judicial sentence; to settle or decide by choice of alternatives or possibilities; . . . to come to a decision. . . ." *Id.*, at 226.

Because the legislature gave the department the same latitude in reviewing a taxpayer's returns after a federal audit had begun as the department had initially within the original three year examination period, the conclusion would seem inescapable that the department is not limited to a mere *recomputation* of the taxpayer's Iowa liability based upon newly developed federal figures (emphasis added). The department is accorded the authority, as they are in the first instance, to scrutinize and inspect the Iowa returns and decide and fix the amount of tax liability. Thus it is apparent that the department may challenge Moorman's apportionment formula and the tax liability following from its use in the period beyond the three year limitation as within its powers to both 'examine and determine'.

More supportive still of this conclusion is a focus on another aspect of the six months statutory exception. Regarding the nature of the controversy existing between the taxpayer and Internal Revenue Service, Section 422.25 says ". . . the department shall have six months from the date of final disposition of *any* controversy between the taxpayer and the internal revenue service. . . ." (emphasis added).

We cannot help but believe that the broad powers vested in the department to 'examine and determine' anew after a federal audit had begun were powers then constrained to such duties only if the federal audit produced adjusted income which, in turn, might adjust Iowa taxable income. It is plain that the controversies between the

taxpayer and Internal Revenue Service which can result in application of the department's statutory duties are not just certain controversies whose resolution changes the taxpayer's base for Iowa tax purposes but "any controversy" whether a change affecting Iowa tax results or does not result.

In sum, this Court concludes that the defendant properly made his revised assessment using the statutory formula of Section 422.33 on income attributable to Moorman's fiscal tax years ending March 31, 1968 and 1969.

We turn now to the more onerous task of determining the constitutionality of the 'single factor sales' formula of Section 422.33.

CONSTITUTIONALITY

It is necessary at the outset to review the standards by which the constitutionality of legislation is measured. The principles are well known that

> "(r)egularly enacted statutes are accorded a strong presumption of constitutionality. When constitutionality is merely doubtful [courts] will not interfere as it must be shown that legislative enactments clearly, palpably and without doubt infringe upon constitutional rights before an attack will be upheld. Every reasonable basis of support for a statute must be negated by the attacking party."

State v. *Aldrich*, 231 N.W.2d 890, 894 (Iowa 1975) (quoting, *State* v. *Kueny*, 215 N.W.2d 215 (Iowa 1974)); *Lee Enterprises, Inc.* v. *Iowa State Tax Commission*, 162 N.W.2d 730 (Iowa 1968); *Vilas* v. *Iowa State Board of Assessment and Review*, 223 Iowa 604, 273 N.W. 338 (1937); *Cook* v. *Hannah*, 230 Iowa 249, 297 N.W. 262 (1941).

The burden falls upon the party challenging the statute's constitutionality to negative every reasonable basis upon which the statute might be sustained. *State* v. *Hall*, 227 N.W.2d 192, 193 (Iowa 1975); *Green* v. *Shama*, 217 N.W.2d 547 (Iowa 1974); *Keasling* v. *Thompson*, 217 N.W.2d 687 (Iowa 1974); *Lee Enterprises, supra*, at 238. 84 C.J.S. *Taxation* Section 36 at 121 (1954) ("(t)he presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons or classes.")

In the field of taxation, perhaps more than in any other area, legislatures are accorded the greatest deference in constructing workable taxing mechanisms. *Lehnhausen* v. *Lake Shore Auto Parts Co.*, 410 U.S. 356 (1973). In *Madden* v. *Commonwealth of Kentucky*, 309 U.S. 83, 87-8 (1939) the United States Supreme Court observed:

> "The broad discretion as to classification possessed by a legislature in the field of taxation has long been recognized. This Court fifty years ago concluded that 'the fourteenth amendment was not intended to compel the states to adopt an iron rule of equal taxation,' and the passage of time has only served to underscore the wisdom of that recognition of the large area of discretion which is needed by a legislature in formulating sound tax policies. Traditionally classification has been a device for fitting tax programs to local needs and usages in order to achieve an equitable distribution of the tax burden. It has, because of this, been pointed out that in taxation even more than in other fields, legislatures possess the greatest freedom in classification. Since the members of a legislature necessarily enjoy a familiarity with local conditions which this Court cannot have, the presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is hostile and oppressive discrimination against particular persons and classes. The burden is on the one attacking the legislature arrangement to negative every conceivable basis which might support it." (numerous footnotes omitted).

Mindful as we are of the very delicate and sensitive obligations which we now undertake and fully aware of all presumptions and burdens which run in favor of a declaration of constitutionality of the legislation now at issue, we assume the duty that is ours and turn to the constitutional attack levied by Moorman against Iowa Code Section 422.33. *Marbury* v. *Madison*, 1 (Cranch) 427 (1804).

FACIAL CONSTITUTIONALITY OF SECTION 422.33

Iowa Code Section 422.33 reads:

> *"Corporate tax imposed.* A tax is hereby imposed upon each corporation organized under the laws of this state, and upon every foreign corporation doing business in this state, annually in an amount computed by applying the following rates of taxation to the net income received by the corporation during the income year:
>
> [rates omitted]
>
> "1. If the trade of business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on the portion of the net income reasonably attributable to the trade or business within the state, said net

income attributable to the state to be determined as follows:

"a. Interest, dividends, rents and royalties (less related expenses) received in connection with business in the state, shall be allocated to the state, and where received in connection with business outside the state, shall be allocated outside the state.

"b. Net income of the above class having been separately allocated and deducted as above provided, the remainder of the net income of the taxpayer shall be allocated and apportioned as follows:

. . . .

"Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

"The gross sales of the corporation within the state shall be taken to be the gross sales from goods sold and delivered within the state, excluding deliveries for transportation out of the state."

Iowa Code Section 422.33 taxes corporate net income from the manufacture and sale of tangible personal property using an apportionment method applied to corporations doing business both in the state and out of the state on that portion of net income the statute says is "reasonably attributable" to the business conducted in state. The method described for 'reasonably attributing' net income as between in-state and extra-territorial activity is the fraction defined by manufacturers' in-state sales of tangible personal property, as the numerator, over similar sales of such property made by that manufacturer everywhere

else—the denominator. The resulting fraction is applied to the manufacturer's net income and the result is the income taxable in Iowa. This taxing method is commonly referred to as the 'single-factor sales formula'.

By contrast and for a full understanding of the operation of the single factor sales formula, the apportionment method Moorman employed when filing its tax returns for the years in question is commonly known as the three factor formula. That formula in its operation employs not only sales in Iowa as an indicia of the tax it should pay here but includes two other factors: the payroll of its Iowa personnel and the value of the manufacturer's in-state property holdings. Taking, as an example, then, Moorman's business for its fiscal year ending March 31, 1968, the results in application of the Iowa single sales factor formula and the three factors (sales, payroll, property) formula are seen to produce readily apparent differences in the tax Moorman must pay this state.

For Moorman's fiscal year 1968, it reported total gross sales from all of its operations in this country of $97,719,800. Of that sum, $22,102,015 represented sales in Iowa. Application of the single factor formula results in the fraction of approximately 1/5—as a percentage, 22.6177%. This factor is multiplied against Moorman's net income with the product representing the taxable income to which Iowa applies its rates.

The three factor approach used instead by Moorman works this way: the Iowa sales percentage (22.6177%) is given one-third weight (.33 x 22.6177%), as are the elements of payroll and property. Moorman's Iowa property holdings for that year represent merely 1/25 of the property it owned everywhere—4.0753%. Moorman's payroll for that year amounted to $23,919,381 of which $3,-

739,426 was paid to its Iowa salesmen and warehousemen. As a fraction between 1/6 and 1/7 of its entire year's payroll went to Iowa wage earners—15.6335%. The property factor and payroll factor are given equal weight with the sales factor so that the weighted percentage applied to Moorman's net income for that year is: (.33 x .226177) + (.33 x .40753) + (.33 x .156335) or .141088, or 14.1088%. This decimal contrasts sharply with the product gained from the single sales factor alone; here .226177.

When these respective products are applied against Moorman's net income for the fiscal year of 1968, the determination would yield—as should readily be clear—Iowa taxable income of $1,548,284 and not the $998,411 which would follow from applying the evenly weighted three factor product. The difference between the formulae applied result in a difference to Iowa of some $549,873 of taxable income and to Moorman in many thousands of dollars in additional tax liability.

These figures show roughly the contrast between the apportionment mechanism Moorman used from 1968 through 1972 and the one later applied by the defendant. Against this backdrop we proceed to the individual constitutional arguments Moorman makes.

EQUAL PROTECTION

Moorman assails the single sales factor tax apportionment method as in violation of the equal protection clause of the Fourteenth Amendment to the United States Constitution and the similar clause in the Iowa Constitution, Article I, Section 6. It contends the classifications established by Section 422.33 invidiously discriminate against it and in favor of solely Iowa based manufacturers who ship most or all of their goods out of state since all of

plaintiff's sales in state are taxed at 100% and those of hypothetical Iowa manufacturers who ship totally out-of-state are not taxed in Iowa at all.

When constitutional provisions of both the federal Constitution and Iowa Constitution contain a similar guarantee, "they are usually deemed to be identical in scope, import and purpose", and cases interpreting the federal standard are consulted "for such light and guidance as they may afford." *Davenport Water Company* v. *Iowa State Commerce Commission*, 190 N.W.2d 583, 593 (Iowa 1971).

In determining whether legislative treatment of various objects sought to be addressed within a statutory scheme violates equal protection, the United States Supreme Court has said:

> "'1. The equal protection clause of the Fourteenth Amendment does not take from the State the power to classify in the adoption of police laws, but admits of the exercise of a wide scope of discretion in that regard, and avoids what is done only when it is without any reasonable basis and therefore is purely arbitrary. 2. A classification having some reasonable basis does not offend against that clause merely because it is not made with mathematical nicety or because in practice it results in some inequality.'" *Morey* v. *Doud*, 354 U.S. 457 (1957) (citing *Lindsey* v. *Natural Carbonic Gas Co.*, 220 U.S. 61 (1911)).

We look to the statute to determine the nature of classifications it prescribes.

Section 422.33, The Code, imposes a tax "upon each corporation organized under the laws of this state, and

upon every foreign corporation doing business in this state. . . ."

It is readily apparent that the statute in question focuses on the classification of 'corporations'. Since classifying corporations for different tax treatment than individual persons has most recently been sustained in *Lehnhausen* v. *Lake Shore Auto Parts Co.*, 410 U.S. 356 (1973), the Iowa scheme taxing corporations cannot be challenged merely because corporations are taxed. Nor does the fact that Section 422.33 establishes a graduated tax on corporate incomes lead to a finding of an invidious classification, for all corporations, without regard to any other factors, have been taxed by the same apportionment mechanism—the single sales factor. See *Illinois Central Ry. Co.* v. *Minnesota*, 309 U.S. 157 (1940). The simple matter is that for purposes of classification, the legislature has singled out the income of all "corporations" as the basis on which the single sales factor is to apply; and while application of the formula yields differing amounts of tax due, for equal protection analysis, all corporations are similarly situated and are accorded exactly the same tax treatment.

This Court concludes that Iowa Code Section 422.33 on its face creates no classifications which may be found to violate Moorman's rights to equal protection of the law under either the Fourteenth Amendment of the United States Constitution or Article I, Section 6 of the Iowa Constitution. Indeed, Moorman's complaints concerning the operation of Section 422.33 would seem to be complaints shared by all corporations taxed by the statute whose operations are multi-state in extent. To that end Moorman's next attack is premised on the due process clauses of both Iowa and United States Constitutions.

DUE PROCESS

In approaching Moorman's due process assignments we are haunted by the unquieted spirit of *Lochner* v. *State of New York*, 198 U.S. 45 (1905). It is remarked that if we find the single sales factor statute unconstitutional, our judgment should address which of the myriad of tax formulae currently in use should be that Iowa is left to follow. If it is decided the present statute is unconstitutional, we are petitioned to point the way our taxing systems should be written.

We decline this invitation as it has been rejected so many times before (*West Coast Hotel Co.* v. *Parrish*, 300 U.S. 379 (1937); *Olsen* v. *State of Nebraska*, 313 U.S. 236 (1941); *Lincoln Federal Labor Union* v. *Northwestern Co.*, 335 U.S. 525 (1949); *Giboney* v. *Empire Storage Co.*, 336 U.S. 490 (1950); *Williamson* v. *Lee Optical Co.*, 348 U.S. 483 (1955)) and note that this Court is not ordained to sit as the "super legislature" of a prior era in testing the ". . . wisdom, need, and propriety of laws that touch economic problems, business affairs, or social conditions." *Griswold* v. *State of Connecticut*, 381 U.S. 484 (1965); *City National Bank of Clinton* v. *Iowa State Tax Commission*, 251 Iowa 603, 102 N.W.2d 381 (1960); 51 Am. Jur. *Taxation* Section 47 (1944). We determine only whether Section 422.33 is unconstitutional.

In subjecting Moorman's arguments to due process scrutiny the initial inquiry must be whether "the taxing power exerted by the state bears a relation to protection, opportunities and benefits given by the state. The simple but controlling question is whether the state has given anything for which it can ask return." *State of Wisconsin* v. *J. C. Penney Co.*, 311 U.S. 435, 444 (1940). As said in *Northwestern States Portland Cement Company* v. *State*

of Minnesota, 358 U.S. 450, 464-5 (1959) denying plaintiff's 'due process' attack,

> "The taxes [there] imposed are levied only on that portion of the taxpayer's net income which arises from its activities within the taxing state. These activities form a sufficient 'nexus between such a tax and transactions within a state for which the tax is an exaction.' *State of Wisconsin* v. *J. C. Penney Co.,* [supra]. It strains reality to say, in terms of our decisions, that each of the corporations here was not sufficiently involved in local events to forge 'some definite link, some minimum connection' sufficient to satisfy due process requirements."

See also *General Motors Corporation* v. *State of Washington,* 377 U.S. 436 (1964); 51 Am. Jur. *Taxation* Section 92 (1944).

Of course, Moorman, first and foremost, is accorded the not invaluable right to do business in the State of Iowa. The record shows its sales in Iowa are substantial. It is given the protection of Iowa laws with resort to the Iowa court system if it determines court powers are needed to protect its corporate rights—as here. It is certain that Moorman's business presence and activities in Iowa with this State's consent constitute the "minimum connection" by which Iowa can constitutionally levy a corporate tax.

The more narrow question presented, however, acknowledging that ". . . the tax in practical operation has relation to opportunities benefits [and] protection conferred or afforded by [Iowa is whether] the tax is fairly apportioned to the commerce carried on within [this State]." *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission,* 390 U.S. 317, 325 (1968) (fn. 5).

Said further by the *Norfolk & Western Railway* Court, addressing a Missouri *ad valorem* tax on railroad rolling stock

> "In some cases the Court has concluded that States have, in fact, cast their tax burden upon property located beyond their borders. [citing cases] The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due.[5] A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to 'project the taxing power of the state plainly beyond its borders.' [cited case] Any formula used must bear a rational relationship, both on its face and in its application, to property values connected with the taxing State."

We return to the facts of Moorman's tax predicament to determine whether the State of Iowa imposes its tax on activities fairly apportioned to Moorman's presence here or whether the single sales factor tax demands more than this State can rightfully ask.

It is useful at this point to remember that while Moorman's sales in Iowa constitute roughly one-fifth of its total interstate sales, all of the goods sold in Iowa are manufactured in Illinois. Taking Moorman's fiscal tax year of 1968 again, Moorman contends, respecting the Illinois manufactured goods sold here, that the Iowa tax recognizes none of the manufacturing inputs (payroll and property) of the Illinois process and taxes only the final end and *raison d'etre* of its production efforts; e.g. sales. Thus Moorman asserts that factors, at least as valuable as sales

used in determining the proportion of taxes it should pay to this State, are left entirely out of the Iowa tax equation. It submits this documentation: For its fiscal year of 1968 the percentage of Moorman's payroll associated with its Illinois operations was 41% of its payroll everywhere; the Iowa payroll percentage was 15.63%. Of its property everywhere, that located in Illinois represented 84.29%, while that in Iowa was a mere 5.27%. Finally its sales in Iowa for that year were 21.88% of its sales everywhere. Yet in light of Moorman's relatively small property holdings and payroll contributions in Iowa (none of which are attributable to the manufacture of goods sold here), this State taxes 100 percent of in-state sales (21.88% of income for 1968), which are to a greatest degree attributable to Illinois plant and personnel inputs. Put slightly different, considering total Iowa and Illinois property and payroll alone, Iowa payroll represents but 27.61% while Illinois payroll, substantially higher, runs at 72.39% of total payroll between these two states. Illinois property predominates in balance with 94.11% located here as between it and this state; Iowa property remains only a miniscule 5.89%. But because the Iowa single sales factor tax admits of neither the property nor payroll inputs of Illinois plant and labor as part of its formula, each dollar in sales of Moorman's goods in Iowa is taxed at 100% while nearly 75% of Moorman's payroll and 30% of its capital is used in the manufacture of the goods taxed here.

While accepting the right of Iowa to tax its corporate income for the services this State renders, it maintains that Iowa cannot tax *all* of Moorman's income because only a small proportion of servicing inputs arise from its relation with this State. Since the largest quantum of capital and labor respecting its product sold here results

from its Illinois relationship, the Iowa apportionment formula fails to reasonably apportion profits traceable to Illinois operations and taxes those activities occurring in Illinois. In this sense, says Moorman, the single sales factor taxes more than that which should be fairly apportioned to Iowa and, as a consequence, violates its constitutional rights of due process under both United States and Iowa Constitutions.

We agree.

Perhaps the closest to confirmation of the holding here reached comes from *General Motors Corporation* v. *District of Columbia*, 380 U.S. 553 (1965). At issue there was a regulation formulated by the Tax Commissioners of District of Columbia pursuant to the District of Columbia Income and Franchise Tax Act of 1947. The statute provided that "(t)he measure of the franchise tax shall be that portion of the net income of the corporation . . . as is fairly attributable to any trade or business carried on or engaged in within the District and such other net income as is derived from sources within the District." .The Commissioner's regulation, however, taxed income from the sale of tangible personalty for any particular year on the basis of a single sales factor, which operated in the same manner as Iowa's formula. In striking the regulation as exceeding the statutory authorization permitting a tax only on income "fairly attributable" to the District of Columbia, the Supreme Court left no doubt that the single sales factor apportionment method transgressed more than the statute at issue. Through the discriminating use of dicta, that Court marked the single sales factor formula as potentially violative of constitutional guarantees, although stating they took no position as to the constitutionality of a state tax scheme premised on the use of the single sales factor alone. *Id.*, at 561.

While the constitutional implications of that decision extend more to problems associated with violation of the Commerce Clause (of which more later), so far as 'due process' is here concerned, the Court commented:

> "The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporations income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves." *Id.*, at 559-60.

The plaintiff in that case, General Motors Corporation, stood in exactly the same position as plaintiff here. General Motors' sales in the District of its automobiles were in the millions of dollars and the District tax was imposed upon 100% of such sales. The manufacturing process in that case however, like here, was conducted totally outside the District. The concern the *General Motors* court had with the use of the single sales factor formula was that of the reasonableness of apportionment. Speaking more to Commerce Clause issues, the Court made clear that taxing schemes must fairly apportion corporate incomes so that multiple taxation does not result, as we have found it does in this case.

Finding that Iowa Code Section 422.33 imposes taxes on business activity carried on outside Iowa borders, and therefore violates 'due process', we move on to consider the Commerce Clause assignments.

COMMERCE CLAUSE

In *Northwestern States Portland Cement Company* v. *State of Minnesota*, 358 U.S. 450 (1959) the Supreme Court was called upon to determine the constitutionality of state net income tax laws which levied taxes on that portion of an out-of-state corporation's net income earned in and fairly apportioned to business activity in the forum state. The attack made centered on 'commerce clause' and 'due process' questions. Reviewing the appropriate 'commerce clause' standards the Court detailed:

> "It has long been established doctrine that the Commerce Clause gives exclusive power to the Congress to regulate interstate commerce, and its failure to act on the subject in the area of taxation nevertheless requires that interstate commerce shall be free from any direct restrictions or impositions by the States. Gibbons v. Ogden, 1824, 9 Wheat. 1, 6 L.Ed. 23. In keeping therewith a State 'cannot impose taxes upon persons passing through the state, or coming into it, merely for a temporary purpose' such as itinerant drummers. [case cited]. Moreover, it is beyond dispute that a State may not lay a tax on the 'privilege' of engaging in interstate commerce [case cited]. Nor may a State impose a tax which discriminates against interstate commerce either by providing a direct commercial advantage to local business [cases cited], or by subjecting interstate commerce to the burden of 'multiple taxation' [cases cited]. Such impositions have been stricken because the States, under the Commerce Clause, are not allowed 'one single tax-worth of direct interference with the free flow of commerce.' [case cited]." *Id.*, at 458.

For many intents and purposes, the test of a state's taxing law for Commerce Clause analysis is the same as it is for 'due process' purposes. Thus, as said in *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission, supra,*

> "The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due.[5]
>
> * * *
>
> [fn. 5] We have said: "The problem under the Commerce Clause is to determine 'what portion of an interstate organism may appropriately be attributed to each of the various states in which it functions.' . . . . So far as due process is concerned the only question is whether the tax in practical operation has relation to opportunities, benefits, or protection conferred or afforded by the taxing State." 390 U.S., at 325.

Consideration of these Commerce Clause strictures requires, as it did with 'due process' investigation, that the Iowa single sale factor apportionment method be shown that its application ". . . has resulted in such gross overreaching, beyond the values represented by the intrastate [activity] purported to be taxed, as to violate the Due Process and Commerce Clauses of the Constitution." *Id.*, at 326.

We have seen, considering Moorman's 'due process' challenge above, that the Iowa apportionment method, in taxing plaintiff's in-state sales, imposes taxes on factors at least as valuable as the 'sales' criterion. These factors

were identified as Moorman's capital and labor or in terms of a three factor formula—property and payroll. And as this case on its facts clearly displays, all of Moorman's property and payroll used to produce the livestock products sold here are located in Illinois. As we found above and in terms of scenario posed in *General Motors Corporation* v. *District of Columbia,* supra, at 559-60:

> "The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves."

Since Illinois taxes apportion corporate income using the three factor apportionment method, S.H.A., Sections 120-3-304 612-(3), Moorman finds its income taxed by both Iowa and Illinois exactly as the *General Motors* Court described.

We find and hold that the single sales factor of Iowa Code Section 422.33 taxes values beyond those which may be justly allocated to intrastate Iowa activity; and application of the formula results in "gross overreaching" by this State of conduct interstate in character. We conclude Iowa Code Section 422.33 on its face violates the Commerce Clause to the United States Constitution.

Another aspect of the Commerce Clause is implicated by the Iowa taxing mechanism; the burden cast upon interstate commerce by the spectre of "multiple taxation." *J. D. Adams Mfg. Co.* v. *Storen,* 304 U.S. 307, 311-12 (1938), striking an indiscriminate and unapportioned 'privilege'

tax on gross receipts from commerce, put the rule this way:

> "The vice of the statute as applied to receipts from interstate sales is that the tax includes in its measure, without apportionment, receipts derived from activities in interstate commerce; and that the exaction is of such a character that if lawful it may in substance be laid to the fullest extent by states in which the goods are sold as well as those in which they are manufactured. Interstate commerce would thus be subjected to the risk of a double tax burden to which intrastate commerce is not exposed and which the commerce clause forbids. We have repeatedly held that such a tax is a regulation of, and a burden upon, interstate commerce prohibited by Article I, Section 8 of the Constitution."

In recent years a pall has been laid upon the *Adams Mfg.* "risk" of multiple taxation test. The suggestion was made in *General Motors Corporation* v. *Washington,* 377 U.S. 436 (1964) that the mere 'risk' of a taxpayer's income being subjected to double taxation would have to give way to an actual showing that the income, in fact, was bearing taxation from multiple sources. The Court of Appeals of Michigan was confronted with these differing standards in *Michigan Fruit Canners, Inc.* v. *Michigan Department of Treasury,* 53 Mich. App. 1, 218 N.W.2d 385 (1974). That Court considered a Commerce Clause challenge to Michigan's single sales factor franchise tax. Regarding the *Adams* 'risk' rule the Michigan Court noted the most recent United States Supreme Court pronouncement on the subject, *Evco* v. *Jones,* 409 U.S. 91 (1972), revitalized *Adams* and in so doing paid no regard to *General Motors Corporation* v. *Washington,* supra. The Michigan Court concluded the *Adams* rule respecting the risk

of multiple taxation remained "the" rule and applied it to the facts of that case.

Our reading of *Evco* v. *Jones,* supra, compels us to agree with the Michigan Court that *Adams* is the test that must be applied here; although we note that if the Iowa single sales factor apportionment method were sustained by this opinion, both the *Adams* 'risk' test and the *General Motors Corp.* v. *Washington* 'actual taxation' tests would be met.

The facts surrounding Moorman's tax dilemma once again become crucial in demonstrating that Iowa Code Section 422.33 runs afoul of the Commerce Clause "multiple taxation" prohibition.

Looking to Moorman's tax year of 1968 it appears that the corporation's apportionable income (that amount to which the single sales factor is applied and whose product results in Iowa taxable income) for that year amounted to $7,076,510. Since Moorman's Iowa sales relative to sales everywhere were 21.8792%, Iowa taxable income in that year, by statute, should have been $1,548,284. This is the dollar-figure subjected to taxation through use of the single sales factor.

The rub is that Illinois, by use of its equally balanced three factor formula, reserves the right to tax income resulting from Iowa sales because it is in Illinois that the manufacturing process respecting goods sold here occurs—in the form of Illinois property and payroll.

Moorman submits these statistics, to which defendant has stipulated, to show in a compelling manner the taxes both States impose on the same income: For 1968, Moorman's Illinois payroll was equal to 41.00% of its total payroll. For the same year, its property in Illinois amounted to 84.29% of all property it owned. Since the

sales element of the Illinois three factor apportionment formula for 1968 was 0.00% (because only Iowa sales are at issue), Illinois will apportion 41.76% ((.33 x 41.00%) + (.33 x 84.29%) + (.33 x 0.00%)) of income from Iowa sales ($1,548,284) upon which it will apply its tax rate. Upon this same 1968 income, Iowa will impose its tax rates on 100% of that amount.

Thus the percentage of Moorman's 1968 income from Iowa sales taxed by Iowa (100%) added to the percentage of the same income Illinois would tax (41.76%) yields the total percentage of income which must bear a corporate tax between these two states: 141.76%. Applying this sum to Moorman's income from Iowa sales in that year ($1,548,284) makes clear that Moorman, in effect, pays taxes on a hypothetical $2,194,847 when their real dollar income stood at the reported $1,548,284. The amount of sales income bearing the tax burden of these two states in excess of Moorman's Iowa sales income is $646,563

It is this amount (141.76% of real income or $646,563) this Court finds to impermissibly infringe upon Commerce Clause protections. It will not do to say: "The Constitution is not a formulary." (*State of Wisconsin* v. *J. C. Penney,* 311 U.S. 435, 444 (1940)) or to say: "There is nothing in the Constitution which requires a state to adopt the best possible system of taxation." (New York v. Latrobe, 279 U.S. 421, 427 (1929)) when the outcome is as gross and disproportionate as these figures show.

It is upon our return to the teaching of *General Motors Corporation* v. *District of Columbia,* supra, that Justice Stewart's words take on added meaning and leave no doubt of their constitutional intonation: "The use of an apportionment formula based wholly on the sales factor in the context of general use of the three-factor approach will

ordinarily result in multiple taxation of corporate net income. . . ." 380 U.S. at 559.

So with this case.

In rejoinder, it is asserted the Supreme Court has on many different occasions in the past upheld the use of single factor taxing apportionment formulae. Cited are: *Underwood Typewriter Co.* v. *Chamberlain,* 254 U.S. 113 (1920); *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission,* 266 U.S. 271 (1924); *National Leather Co.* v. *Massachusetts,* 277 U.S. 413 (1928); *Kent-Coffey Mfg. Co.* v. *Maxwell,* 204 N.C. 365, 168 S.E. 397 (1933) *aff'd* 291 U.S. 642 (1933); and *Ford Motor Co.* v. *Beauchamp,* 308 U.S. 331 (1939). But the common thread running between all cases cited, their age, limits their significance here. To that the Supreme Court made express reference in *General Motors Corporation* v. *District of Columbia,* supra. In observing that multiple taxation of corporate net income was the effect of using the single sales factor approach, the Court drew that conclusion from the fact that the context of states' corporate tax laws in 1965 was generally oriented to the three-factor formulae. Of the thirty-eight states in 1965 levying tax on corporate incomes, twenty-six states used an equally-weighted three factor approach, three others used a substantially similar three factor vehicle. Another three used the two factor sales-property formula and only four taxed income on the basis of geographically defined sales. 380 U.S. 559, fn. 9.

Today the context is even more exaggerated. Of forty-six states levying taxes on corporate income (Nevada, South Dakota, Texas and Wyoming have no corporate income tax) only one, Iowa, retains the use of the single sales factor. In this light, it cannot remain arguable that the caveat sounded by the *General Motors* Court has the impact of mere dicta.

We find and hold that Iowa Code Section 422.33, on its face, threatens the risk of multiple taxation of Moorman's income thereby unduly burdening interstate commerce in violation of Article I, Section 8, Clause 3 of the United States Constitution.

Yet another facet of the Commerce Clause impales the Iowa apportionment method following from the line of cases of *Nippert* v. *City of Richmond*, 327 U.S. 416 (1946) and *Memphis Steam Laundry Cleaner* v. *Stone*, 342 U.S. 389 (1952). These cases may be construed as stating the rule that Commerce Clause protections are violated by burdening the free flow of interstate commerce when State law or municipal ordinance discriminatorily grants to local enterprise benefits which are withheld from interstate competitors.

While Moorman's business in Iowa is subjected to the double tax of both Iowa and Illinois, a similarly situated Iowa interstate manufacturer shipping goods, for example, to Illinois would pay taxes only in Illinois; then on the one-third portion of its business activity there represented by its Illinois sales. Assuming the Iowa based manufacturer made all of its sales extra-territorially, Iowa, because of the single sales factor, would tax none of the activity (represented by sales) that were made in Illinois. The obvious commercial advantage to the Iowa based manufacturer is that it would pay no tax here and be required in a three factor jurisdiction to pay tax merely on the sales component of its business conduct there. Justice Stewart comments on this aspect of the result of single-factor apportionment, saying:

> "Conversely, in some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in three-factor jurisdictions so that only 33% of their incomes will be subject to state taxation. In any case, the sheer inconsistency of the District formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and uneconomic pattern of plant location, and so presents an added reason why this Court must give proper meaning to the relevant provisions of the District Code." 380 U.S., at 560.

It is thus clear that the Iowa Code Section 422.33 single sales factor apportionment method contravenes the Commerce Clause in ways manifest above; and we so hold.

SAVINGS CLAUSE

In view of our holding that Iowa Code Section 422.33(1)(b) is facially unconstitutional for the reasons found above, this Court has serious reservations as to whether Iowa Code Section 422.33(2), allowing the director the discretion of applying a different apportionment formula if the result of application of the single factor formula is inequitable, can operate as a "savings clause" in view of our holdings.

Assuming *arguendo* that Section 422.33(2) could so operate, we observe that of 1,969 corporate income tax returns filed by non-Iowa manufacturers between the years 1968 through 1972 inclusive, the director has allowed only one such corporate taxpayer the privilege of using the three-factor payroll-property-sales apportionment formula expressly condoned by the *General Motors Corporation* v. *District of Columbia*, supra, Court. In balance it must be stated that of the 1,969 corporate tax returns filed for those years the director did authorize use of other apportionment formulae which were neither the single sales factor nor the three factor formula for 90 corporate taxpayers.

We conclude on these facts concerning non-Iowa manufacturers, that the largely unexercised discretion granted the director to exempt a taxpayer from the reach of Iowa Code Section 422.33 cannot save the statute from its remaining unconstitutional infringements respecting corporations not granted license, and from its timely death by this opinion.

SUMMARY OF CONCLUSIONS OF LAW

In view of the factual findings made by this Court throughout this opinion, we conclude:

(1) that Iowa Code Section 422.25 authorizes the defendant to examine and determine Moorman's tax liability for its fiscal years of 1968 and 1969 notwithstanding the three year bar of this section;

(2) that Iowa Code Section 422.33(1)(b) does not violate the Equal Protection Clauses of either United States Constitution or Iowa Constitution;

(3) that Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Due Process Clauses of both the United States Constitution and Iowa Constitution; and

(4) that Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Commerce Clause, Article I, Section 8, Clause 3, of the United States Constitution because it

(a) does not fairly apportion interstate business activity to intrastate tax values;

(b) causes multiple taxation of corporate net income by more than one taxing jurisdiction; and

(c) provides local business with a direct commercial advantage not so enjoyed by interstate business.

(5) that the apportionment percentages to be applied to Moorman's net income for the tax years in controversy in this action shall be those specified in paragraph thirty-four of the stipulation.

In response to these parties' request, no decree is now provided and the Court retains jurisdiction of this matter for ninety days within which time these parties shall come to some agreement as to the amount of Moorman's tax liability. If such agreement is not reached within said period, to begin with the filing of this opinion, the Court shall be notified within five days of the expiration of said period and such further proceedings as are necessary to the decree shall at that time be scheduled.

/s/ A. M. Critelli
Judge, Fifth Judicial District of Iowa

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IN THE DISTRICT COURT OF THE STATE OF IOWA
In and for Polk County

EQUITY NO. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

RULING ON JOINT MOTION TO RECONSIDER AND SUPPLEMENTAL FINDINGS

(Filed January 7, 1977)

NOW on this 7th day of January, 1977, the above-captioned matter coming on for hearing before the undersigned on the joint oral motion of the parties, the plaintiff represented by Walter R. Brown and John V. Donnelly, the defendant by Harry M. Griger, and amicus curiae, Iowa Manufacturers Association, by James L. Rogers and Russell L. Samson, the Court having heard legal arguments of counsel and after consideration of additional authorities cited to the Court is now prepared to respond to said joint motion.

On the 17th day of December, 1976, this Court filed its findings of fact and conclusions of law in this matter. Since that time these parties have had an opportunity to examine said findings and conclusions and questions have been raised as to the scope and effect of said ruling. In light of these questions the Court believes some modification of its earlier ruling is now in order.

The requests by counsel for clarification appear to fall along four rough lines of inquiry. Each of these general areas will be separately identified and addressed below.

CORRECTED FINDINGS OF FACT

As part of its findings of fact the Court observed at page 27 of its opinion ". . . that of 1,969 corporate income tax returns filed by non-Iowa manufacturers between the years 1968 through 1972 inclusive, the director has allowed only one such corporate taxpayer the privilege of using the three-factor payroll-property-sales apportionment formula expressly condoned by the *General Motors Corporation* v. *District of Columbia*, supra, Court. In balance it must be stated that of the 1,969 corporate tax returns filed for those years the director did authorize use of other apportionment formulae which were neither the single sales factor nor the three factor formula for 90 corporate taxpayers."

To adequately reflect the facts part of the stipulation, the Court hereby strikes the above quoted language beginning with "In balance . . ." to the end of that paragraph and modifies and expands said ruling by finding the following:

> Of the 1,969 corporate tax returns filed in those years, 91 taxpayers filed on the basis of some other allocation method than the single sales factor. One taxpayer, referred to above, was expressly authorized the use of a three factor formula, while 84 taxpayers were denied resort to three factor apportionment by the director; and three taxpayers made unconsented use of a three factor formula which was put beyond challenge by operation of the statute of limitations.

SCOPE OF UNCONSTITUTIONALITY

Because the Court's December 17, 1976, ruling in this matter leaves questions to these parties' minds on the exact portions of Iowa Code Section 422.33 which was in fact declared to be unconstitutional in said ruling, the Court further delineates the specific aspect of Section 422.33 found to be infirm.

While expressed in the original ruling to be Section 422.33(1)(b) which the Court found defective, the specific portion of Section 422.33(1)(b) which was at issue and found facially unconstitutional was the third full paragraph of that section reading as follows:

> Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

Thus, the balance of Section 422.33 remains unaffected, hence valid, by the December 17 ruling.

THE VALIDITY OF REMAINING PORTIONS OF SECTION 422.33 AS A VIABLE TAXING STATUTE

In light of the confined parameters of this Court's December 17, 1976 ruling the question has been presented as to whether the remainder of Section 422.33 leaves the State of Iowa with a viable corporate taxing statute.

We think the answer to be clear and certain that the unaffected remainder of Section 422.33 itself presents a workable and valid taxing power without regard to the now excised sales factor apportionment method. That conclusion is premised on the language of Section 422.33(1).

Section 422.33(1) states:

> If the trade or business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income, but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on that portion of the net income reasonably attributable to the trade or business within the state. . . .

Since Moorman will now be required to apportion their prior years' income on the basis of the percentages found in paragraph 34 of the stipulation the amount Moorman shall hereinafter apportion to the State of Iowa is identified in the above quoted portion of 422.33(1) as that which is "reasonably attributable" to the trade or business Moorman conducts within Iowa borders. No serious question remains that the standard of Section 422.33(1) defining the income thus to be apportioned as that "reasonably attributed" to Iowa presents constitutional problems. The 'reasonably attributable' apportionment method identified there and in Section 422.33(2) presents a legitimate method of allocating income even without regard to the now stricken but more specific 'sales factor' method existing merely as the legislatively constructed mechanism by which reasonable attribution was measured. The 'reasonably attributable' apportionment method remaining as vital as ever poses no problems for a standard sufficient to withstand full constitutional scrutiny. *Elk Run Telephone Company* v. *General Telephone Company*, 160 N.W.2d 311 (Iowa 1968).

Standing as it does, Iowa Code Section 422.33 leaves the defendant full power to apportion and tax plaintiff's income.

PROSPECTIVE OPERATION OF COURT'S RULING

Fully aware of the immediate and far reaching ramifications of the December 17 ruling, the Court is inclined to believe some pronouncement as to the application of the ruling should be made.

Evidence presented by the defendant in light of our earlier ruling shows compellingly the damage to state finances and efficient government that will result if this ruling is left to operate in its full retrospective breadth. We are convinced by such evidence and awakened to the serious and far reaching consequences such a looming catastrophe presents to this State.

We are not however without power to limit the damage that surely will be visited upon the public fisc. Increasingly courts have been called upon to limit the effect in the change of the construction of a statute by announcing the operation of the new rule of law as prospective only. See *Lemon* v. *Kurtzman*, 411 U.S. 192 (1973) and *Linkletter* v. *Walker*, 381 U.S. 618 (1965). And increasingly it has been recognized that prospective application of a new rule should apply as well to cases sounding of constitutional import. *Linkletter*, at 628. That view is premised on the reality that a ruling of unconstitutionality "is an operative fact and may have consequences which cannot justly be ignored. The past cannot always be erased by a new judicial declaration." *Chicot County Drainage District* v. *Baxter State Bank*, 308 U.S. 371, 374 (1940).

Iowa cases have recognized that a court may make a decision operational on a prospective basis alone. That rule announced in *State* v. *Knox*, 186 N.W.2d 641 (Iowa 1971) is not by its terms limited to cases involving criminal conduct. See also, *Linkletter* v. *Walker*, supra, at 627;

21 C.J.S. *Courts* Section 194 at 327-28 (Supp. 1976). Nor should the rules be different in a case such as this.

It has been long recognized by similar cases from other jurisdictions that the particular urgencies attending public financial well-being and the threatened fiscal embarrassment if not insolvency of public institutions created by a ruling of unconstitutionality require that the new rule of law be mediated in its rigor by a declaration of the scope of its operation. *City of Tempe* v. *Del E. Webb Corporation*, 284 P.2d 477 (Ariz. 1971); *Southern Pacific Company* v. *Cochise County*, 377 P.2d 770 (Ariz. 1963); *Oklahoma County* v. *Queen City Lodge No. 197, I.O.O.F.*, 156 P.2d 340 (Okla. 1945); 21 C.J.S. *Courts* Section 194 (b) (1940, Supp. 1976).

We believe the overriding equities presented favor the defendant's view that the Court's ruling herein be limited to operating only in a prospective manner. But we find and hold that plaintiff Moorman should have the benefit of the ruling it generated.

We therefore find and hold that the Court's ruling herein which holds the third full paragraph of Iowa Code Section 422.33(1)(b) facially unconstitutional shall be applied prospectively, with the exception that this holding shall apply to Moorman.

The benefit of this ruling shall not be granted to those corporations who have not taken or can take no timely steps to assert or protect their rights by virtue of the filing of a claim for refund, pursuant to Iowa Code Section 422.73, or protest, pursuant to Iowa Code Section 422.28. But a taxpayer who has so protected or may so protect his rights whether by appeal, judicial review, protest, or claim for refund shall be entitled to a refund of tax paid on only that amount resulting from the dif-

ference in application of the single sales factor method of apportioning that taxpayer's income and other constitutionally appropriate apportionment formulae applied with the consent of the defendant's director. Iowa Code Section 422.33(2).

/s/ A. M. Critelli
Judge, Fifth Judicial District of Iowa

Original filed

Copies to:

Walter R. Brown
John V. Donnelly
Harry M. Griger
James L. Rogers
Russell L. Samson

IN THE DISTRICT COURT OF THE STATE OF IOWA
In and for Polk County

EQUITY NO. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

JUDGMENT AND DECREE

(Filed January 7, 1977)

NOW on this 7th day of January, 1977, this matter comes before the Court for purposes of entry of a judgment and decree upon which an appeal can immediately result, and the Court, being fully advised in the premises, hereby concludes as follows:

IT IS ORDERED, ADJUDGED, AND DECREED that the Court's Findings of Fact and Conclusions of Law, dated December 17, 1976, as modified and supplemented by the Court's Supplemental Findings, dated January 7, 1977, be incorporated herein by reference as if set forth in full.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that defendant have judgment against plaintiff for $3,975 Iowa income tax plus interest of $571 computed through January 31, 1977, for a total of $4,546 and that interest continue to accrue as provided by Section 422.25, Code of Iowa, 1973, until said judgment is paid.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that costs be assessed one-half to plaintiff and one-half to defendant.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that the bond filed herein by plaintiff is hereby discharged.

/s/ A. M. Critelli
Judge, Fifth Judicial District of Iowa

APPENDIX C

IN THE SUPREME COURT OF IOWA

117

60220

MOORMAN MANUFACTURING COMPANY,
Appellee,

v.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Appellant.

(Filed May 25, 1977)

Appeal from the Polk District Court—Anthony M. Critelli, Judge.

The Director of Revenue appeals from ruling of the trial court that the Iowa single-sales-factor formula was facially unconstitutional in violation of due process clauses of the federal and Iowa Constitutions and commerce clause of the federal constitution. Moorman cross appeals from rulings adverse to it.— Reversed on Director's appeal and affirmed on Moorman's cross appeal.

Richard C. Turner, Attorney General, George W. Murray, Special Assistant Attorney General, Harry M. Griger, Assistant Attorney General, for appellant.

Walter R. Brown and John V. Donnelly, of Swift, Brown and Winick, of Des Moines, for appellee.

James L. Rogers and Russell L. Samson, of Rogers and Phillips, of Des Moines, and Philip B. Kurland, Walter

V. Schaefer, and Walter Hellerstein, of Rothschild, Barry & Myers, of Chicago, Illinois, attorneys on brief for Amicus Curiae.

En banc.

MASON, J.

The fundamental issue on this appeal concerns the constitutionality, facially and as applied to the circumstances present herein, of certain provisions of the Iowa corporate income tax scheme. The issue stems from the district court's ruling that the Iowa single-sales-factor formula was facially unconstitutional in violation of due process clauses of the federal and Iowa Constitutions and commerce clause of the federal constitution. The Director of Revenue (Director) appeals from this adverse ruling and plaintiff cross-appeals from rulings adverse to it. The facts were stipulated in the proceedings had in the district court and show the following.

Plaintiff, Moorman Manufacturing Company (hereinafter Moorman), is an Illinois corporation which was doing business in Iowa and elsewhere. Its principal source of income during the fiscal years in question, March 31, 1968 through March 31, 1972, was derived from the manufacture and sale of some 80 different products for feeding livestock and poultry. It is what is commonly referred to as a "unitary" business, that is, its income arises from sources and activities carried on in several states.

During the years involved Moorman had five manufacturing plants located in Illinois, Texas and Nebraska. Its products were sold by more than 2500 salesmen, employees of Moorman, in more than 30 states during the years in question.

It carries on substantial activities in the state of Iowa. With a force of over 500 employees in this state Moorman engages in continuous solicitation of Iowa customers. After sales are negotiated delivery to Iowa customers is typically made from one of the six warehouses that Moorman operates in the state. These warehouses located at Stanwood, Plainfield, Goldfield, Marcus, Atlantic and Knoxville are maintained by Moorman's employees. It did no manufacturing in Iowa. The products that Moorman sells in Iowa are all manufactured in Illinois.

Iowa imposes a tax upon the net income of domestic corporations and foreign corporations doing business in the state. Section 422.33, The Code, 1975. A corporation's "net income" is based upon its "taxable income" as computed for federal tax purposes with an allowance for certain adjustments. Section 422.35. When the trade or business of a corporation is carried on entirely within the state, the corporation is subject to Iowa taxation on the entire amount of its net income. Section 422.33(1). However, when a corporation's trade or business is carried on partly within and partly without the state, it is subject to taxation only on that portion of its net income "reasonably attributable to" the trade or business within the state. Section 422.33(1).

Two computational steps are prescribed by section 422.33(1) for determining that portion of a corporation's net income which is reasonably attributable to its Iowa activities. First, certain income, the geographical source of which is easily identifiable, is allocated to the appropriate state. Section 422.33(1)(a). The second step allocates the remaining net income in one of two ways, depending upon the nature of the corporation's activities. Where, as here, the corporation's income is derived from the manufacture or sale of tangible personal property, the

portion of its net income attributable to its Iowa activities "shall be in that proportion which the gross sales made within the state bear to the total gross sales." Section 422.33(1)(b). The statute defines "gross sales of the corporation within the state" as the "gross sales from goods delivered within the state, excluding deliveries for transportation out of the state." If a taxpayer believes this apportionment formula operates so as to subject him to taxation on a greater portion of his net income than is reasonably attributable to his Iowa activities, provision is made for an application for an alternative method of allocation. Section 422.33(2).

Moorman filed its first income tax return with the state of Iowa for its fiscal year ended March 31, 1949. Pursuant to approval of the Iowa State Tax Commission, Moorman, after allocating its interest, dividends, rents and royalties (less related expenses) within and without the state of Iowa, apportioned the remainder of its net income to the state of Iowa on the ratio that its payroll, property and sales, as computed by Moorman, within the state of Iowa bore to its payroll, property and sales everywhere in the United States, as computed by Moorman, giving equal weight (.33) to its computed payroll, property and sales factors. This method was used by Moorman in each successive income tax return filed with the state of Iowa up to and including the income tax return filed for its fiscal year ended March 31, 1960.

For its fiscal years ended March 31, 1961, 1962, 1963 and 1964, Moorman determined its income from the sale of tangible personal property in this state pursuant to the single-sales-factor formula provided for in section 422.33 (1), The Code, at the direction of the Iowa State Tax Commission.

However, beginning in its fiscal year of 1965 Moorman again applied the three-factor-property-payroll-sales formula in computing its income from the sale of tangible personal property attributable to Iowa and has applied such formula in each succeeding return filed to date, including those filed for the years in issue. The State Tax Commission did not consent to this application of the three-factor formula.

Moorman appealed to the Polk District Court from an order issued by the Director relating to Moorman's corporate income tax returns for its fiscal years ending March 31, 1968, 1969, 1970, 1971 and 1972 which required Moorman to apportion to Iowa for Iowa income tax purposes for those years its net income derived from the manufacture and sale of tangible personal property by use of the single-sales-factor formula provided for in section 422.33 (1)(b), The Code.

Moorman's appeal to the district court involved an attack on the Iowa single-sales-factor formula on three basic grounds which were: (1) The Iowa single-sales-factor formula is facially unconstitutional; (2) The Iowa single-sales-factor formula is unconstitutional, as applied to Moorman's net income; and (3) The failure of the Director to allow Moorman the use of an alternative apportionment formula constituted an abuse of the Director's discretion granted him under section 422.33(2), The Code, 1975.

The three-factor formula employed by Moorman in computing its income from the sale of tangible personal property attributable to Iowa for the years 1968 through 1972 is explained by the Director in his brief and argument in this fashion: A unitary multi-state corporation computes its total net business income from all sources

according to the laws of the taxing state. The corporation then computes a payroll factor, the numerator of which is the payroll in the taxing state and the denominator of which is the total corporate payroll everywhere. The corporation then computes a property factor, the numerator of which is the value of the property in the taxing state and the denominator of which is the total corporate property value located everywhere. Property rented by the corporation from others is generally included in the property factor under special rules. The corporation then computes a sales or gross receipts factor, the numerator of which is the gross sales or receipts in the taxing state and the denominator of which is the total corporate gross sales or receipts everywhere.

In an effort to afford a better understanding of the results of the application of the single-factor formula and the three-factor approach we refer to the following discussion as set forth in the trial court's findings.

Moorman reported total gross sales from all of its operations in this country for the fiscal year 1968 of $97,719,800. Of that sum $22,102,015 represented sales in Iowa. Application of the single-factor formula results in the fraction of approximately 1/5—as a percentage, 22.6177%. This factor is multiplied against Moorman's net income with the product representing the income to which Iowa applies its rates.

The three-factor approach used by Moorman works in this manner: The Iowa sales percentage (22.6177%) is given one-third weight (.33 x 22.6177%), as are the elements of payroll and property. Moorman's Iowa property holdings for the year represent merely 1/25 of the property it owns everywhere—4.0753%. Moorman's payroll for that year amounted to $23,919,381 of which $3,739,426 was paid to its Iowa salesmen and warehousemen. A fraction between 1/6 and 1/7 of its entire year's payroll went to Iowa wage earners—15.6335%. The property factor and payroll factor are given equal weight with the sales factor so that the weighted percentage applied to Moorman's net income for that year is: (.33 x .226177) plus (.33 x 0.40753) plus (.33 x .156335) or .141088 or 14.1088%. This decimal is thus contrasted to the product gained from the single-sales-factor formula alone; here, .226177.

In ruling on Moorman's various contentions, the district court held, in pertinent part, as follows:

"In view of the factual findings made by this Court throughout this opinion, we conclude:

"(1) * * *;

"(2) That Iowa Code Section 422.33(1)(b) does not violate the Equal Protection Clauses of either United States Constitution or Iowa Constitution;

"(3) That Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Due Process Clauses of both the United States Constitution and Iowa Constitution; and

"(4) That Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Commerce Clause, Article I, Section 8, Clause 3, of the United States Constitution because it

"(a) does not fairly apportion interstate business activity to intrastate tax values;

"(b) causes multiple taxation of corporate net income by more than one taxing jurisdiction; and

"(c) provides local business with a direct commercial advantage not so enjoyed by interstate business.

"(5) * * *."

The following is an overview of the issues presented herein by the contentions asserted in both appeals:

1. *Facial Constitutionality—Due Process.*

The Director maintains the district court's determination that the exclusive use of the sales-factor formula for allocating the income of a multi-state corporation to the appropriate states, mandated by section 422.33(1)(b), was, on its face, violative of the due process clauses of the Iowa and federal constitutions, is erroneous as a matter of law. Specifically, the Director maintains Moorman's argument, adopted by the district court, that section 422.33(1)(b) taxes income-producing activities wholly outside the boundaries of Iowa and thus violates the constitutional principle of due process, is not supported by and is contrary to case law authority.

2. *Facial Constitutionality—Commerce Clause.*

As noted, the district court held, on three separate grounds, that section 422.33(1)(b) violated, on its face, the commerce clause of the federal constitution. The Director maintains the "test" used to determine the constitutionality of an income apportionment formula when challenged as violative of due process is the same "test" utilized when such a formula is analyzed with respect to a possible violation of the commerce clause. As a result, the Director's contention that section 422.33(1)(b) does not violate the principle enunciated in the commerce clause is buttressed by the same arguments and authorities set out in the "due process" portion of the Director's brief. Moorman, on the other hand, maintains the district court's determination is well supported by case law authority and is eminently sound.

3. *Facial Constitutionality—Equal Protection.*

The trial court concluded equal protection concepts were not violated by section 422.33(1)(b), on its face. On its cross appeal, Moorman contends the district court's determination was erroneous as a matter of law. Specifically, it is argued the exclusive use of the sales-factor formula results in a corporation being taxed on an amount of its net income which bears no relation to the corporation's activities in the state nor the benefits received by the corporation from the state. Moorman maintains section 422.33(1)(b) "blatantly discriminates" against corporations whose manufacturing facilities are outside of Iowa in light of the fact those corporations are taxed in the same manner as corporations whose manufacturing facilities are located within the state and thus enjoy the benefits afforded them by the state. The Director counters Moorman's arguments by asserting all corporations similarly situated are treated equally by the Iowa scheme. In addition, the Director claims Moorman did not sustain its burden of demonstrating that no rational basis exists for the classifications established by section 422.33(1)(b).

4. *Constitutionality, As Applied—Due Process.*

The district court concluded Iowa's sales-factor apportionment formula was facially violative of the due process clauses of the Iowa and federal constitutions and was likewise contrary to the commerce clause of the federal constitution. In light of that conclusion the trial court deemed it unnecessary to resolve Moorman's contention section 422.33(1)(b), as applied to Moorman, was contrary to principles of due process. The Director, relying upon the fact the trial court looked to the factual circumstances herein demonstrated by the parties' stipu-

lation thereto, contends the district court actually concluded section 422.33(1)(b) was violative of due process as applied to Moorman rather than on its face.

Consequently, it is urged this issue is the crux of the controversy. The Director claims section 422.33(1)(b) is not violative, as applied, of Moorman's due process rights, relying upon the alleged fact Moorman is not "unique" in conjunction with claimed case law support for the validity of this type of apportionment formula. Moorman, however, maintains the district court appropriately analyzed the facial validity of the sales-factor formula and found it wanting with respect to due process concepts. In the alternative, Moorman argues that should this court conclude section 422.33(1)(b) is facially free from constitutional defect, its application to Moorman amounts to a denial of due process, relying upon the arguments posited in the facial due process portion of its brief and argument.

5. *Constitutionality, As Applied—Commerce Clause.*

Again, in light of its ultimate conclusion, the district court did not feel it necessary to resolve Moorman's contention concerning the constitutionality of section 422.33(1)(b), as applied, with respect to the commerce clause of the federal constitution. If this court determines section 422.33(1)(b) is not facially constitutionally defective, Moorman seeks relief by way of this contention, relying upon alleged case law support and its previously referred to commerce clause argument. The Director, again arguing that commerce clause and due process considerations are substantially identical, relies upon his previously referred to commerce clause and due process arguments and maintains no constitutional violation is present under these circumstances.

6. *Constitutionality, As Applied—Equal Protection.*

This issue was not resolved by the district court for the previously referred to reason. Moorman contends application of section 422.33(1)(b) to it results in a denial of equal protection, citing as support therefor the equal protection argument asserted in its challenge to the facial validity of the subject statute. The Director seeks to rebut those contentions by pointing to department of revenue statistics which demonstrate Moorman was not treated differently from other similarly situated taxpayers. In addition, the Director again points to alleged case law support for the proposition that no specific income apportionment formula is constitutionally required.

7. *Constitutionality, As Applied—Article VIII, Section 12, Iowa Constitution.*

Moorman, on cross appeal, points to department of revenue records demonstrating that one foreign manufacturing corporation was permitted by the Director to apportion its net income according to a formula other than that prescribed by section 422.33(1)(b) and argues such fact constitutes a violation of Article VIII, section 12, of the Iowa Constitution, which prohibits such "exclusive privileges." The Director contends that constitutional provision has no application to administrative as opposed to legislative acts, or, in the alternative, cannot serve as the basis for Moorman's requested relief in the absence of a demonstration of discriminatory taxation with respect to similarly situated corporations. No mention of this issue can be found in the district court's ruling.

8. *In ordering Moorman to comply with section 422.33(1)(b), did the Director contravene the duties and responsibilities imposed upon him by section 422.33 and act arbitrarily and capriciously?*

Moorman contends the Director's denial of Moorman's request for an alternative apportionment formula, pursuant to section 422.33(2), violated the duties imposed upon the Director by said section in light of the fact it was clearly demonstrated the sales-factor formula did not result in the allocation to Iowa of that portion of Moorman's net income which was reasonably attributable to Moorman's Iowa business activities. Moorman argues such refusal was the result of a "total abdication of duty" and was arbitrary and capricious. The Director maintains an alternative formula is only available to a taxpayer if the application of the sales-factor approach results in the very constitutional deficiencies which are allegedly involved herein. In other words, it is the Director's position this issue is meaningless in light of the fact any resolution of the constitutional issues involved herein disposes of Moorman's contention. Consequently, the Director again advances his previous constitutional arguments. This issue was not confronted by the trial court.

9. *Retroactivity or prospectivity of a determination section 422.33(1)(b) suffers constitutional deficiencies.*

Resolution of this issue is complicated by a vague record with respect to procedural aspects connected therewith. At this point, suffice it to say Moorman contends this issue is not before this court since it was not raised below. In the alternative, Moorman argues the scope of any decision herein is controlled by section 422.73, which establishes limitations upon the timeliness of refund requests. The Director, on the other hand, argues this court

must define the scope of any determination invalidating section 422.33(1)(b) and posits guidelines in this regard. The district court held its ruling would apply to Moorman and all similarly situated corporations not foreclosed by the time limitations established by sections 422.28 and 422.73.

I. At the outset, this court employs several well settled principles in dealing with questions of a statute's constitutionality:

It is well settled, with notable exceptions not here involved, that all presumptions are in favor of the constitutionality of a regularly enacted statute.

Where the constitutionality of a statute is merely doubtful, this court will not interfere, as it must be shown that legislative enactments clearly, palpably and without doubt infringe upon constitutional rights before an attack will be upheld.

Moorman, as the attacking party, has the burden to demonstrate beyond a reasonable doubt the act violates the constitutional provisions invoked and to point out with particularity the details of the alleged invalidity. To sustain this burden it must negative every reasonable basis which may support the statute. State v. Kueny, 215 N.W.2d 215, 216-217 (Iowa 1974); Sampson v. City of Cedar Falls, 231 N.W.2d 609, 612 (Iowa 1975); State v. Kramer, 231 N.W.2d 874, 879-880 (Iowa 1975); State v. Aldrich, 231 N.W.2d 890, 894 (Iowa 1975); Avery v. Peterson, 243 N.W.2d 630, 633 (Iowa 1976); City of Waterloo v. Selden, ... N.W.2d ....., ... (Iowa 1977).

Keasling v. Thompson, 217 N.W.2d 687, 690 (Iowa 1974), states this principle:

"The judicial branch of the government has no power to determine whether legislative Acts are wise or unwise, nor has it the power to declare an Act void unless it is plainly and without doubt repugnant to some provision of the Constitution. * * * [citing authority]."

In the field of taxation, it would appear the above principles somewhat understate the deference accorded the legislature. In this regard, see 71 Am.Jur.2d, State and Local Taxation, section 96, page 417 and 84 C.J.S., Taxation, section 7, pages 53-54.

In Butler Brothers v. McColgan, 315 U.S. 501, 507, 62 S.Ct. 701, 704, 86 L.Ed. 991, 996, citing authorities, the Court declared that one who attacks a formula of apportionment of income of a corporation doing business in several states carries the distinct burden of showing by "clear and cogent evidence" that it results in extraterritorial values being taxed by the taxing state.

II. As stated, the trial court held the apportionment provision of the Iowa corporate income tax was facially unconstitutional, in violation of due process clauses of the federal and Iowa Constitutions and commerce clause of the federal constitution.

When a corporation's trade or business is carried on partly within and partly without the state, its tax base generally cannot satisfactorily be identified or segregated on a geographical basis. Due to the impracticability of so identifying or segregating the tax base of such a unitary business resort is made to apportionment formulae as a rough means of attributing a reasonable share of the tax base to the taxing state. These considerations are especially pertinent to the taxation of net income, which is at issue here. The net income or profits of a business frequently are "earned by a series of transactions beginning

with manufacture in [one state] and ending with sales in other states," and "[t]he Legislature, in attempting to put upon this business its share of the burden of taxation, [is] faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders." Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 120-121, 41 S.Ct. 45, 46-47, 65 L.Ed. 165, 169.

In regard to the two previously mentioned computational steps prescribed by section 422.33(1) for ascertaining the Iowa portion of the corporation's net income we point out that the initial step is to assign to Iowa the interest, dividends, rents and royalties received in connection with the business inside Iowa and to assign to non-Iowa sources such income received in connection with business outside the state. All income thus assigned is deducted from the overall federally-based determination of net income that would have been taxable by Iowa if the corporation in question had carried on its entire business within the state.

The income which remains after the first step in the statutory procedure is dealt with in one of two ways. In some cases, which are not of concern here, the remaining income may be specifically allocated within and without the state pursuant to rules and regulations promulgated by the director. In other cases the legislature, recognizing the difficulty of specifically allocating to various jurisdictions the net income remaining after assignment of interest, dividends, etc., provided for apportionment of such income to various jurisdictions by an apportionment formula. Accordingly, when corporations are engaged in the manufacture or sale of tangible personal property partly within and partly without the state where there is ordinarily no satisfactory means of determining the pre-

cise jurisdictional source of net income derived for that activity, the statute provides:

"Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales." Section 422.33(1)(b), The Code.

An apportionment formula, whether a single factor, two factor, or three factor, must be applied against a computed net income. The "net income" of a corporation is defined in section 422.35 to include taxable income properly computed for federal income tax purposes under the Internal Revenue Code of 1954 with certain adjustments, one of which is an equitable deduction for 50 percent of federal income taxes paid during the tax or income year.

The Supreme Court has recognized that such formulae, which owe their very existence to the absence of exact alternatives for dividing the tax base of a unitary business, cannot be expected to achieve precision.

"* * * [T]his Court has long realized the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities * * * and has declared that 'rough approximation rather than precision' is sufficient. Illinois Central Ry. v. State of Minnesota, 309 U.S. 157, 161, 60 S.Ct. 419, 422, 84 L.Ed. 670." International Harvester v. Evatt, 329 U.S. 416, 422, 67 S.Ct. 444, 447, 91 L.Ed. 390, 395.

In Nashville, C. & St. L. Ry. v. Browning, 310 U.S. 362, 365-366, 60 S.Ct. 968, 970, 84 L.Ed. 1254, 1256, "* * * the problem to be solved * * * [was] what portion of an interstate organism may appropriately be attributed to each of the various states in which it functions. Basic to the accommodation of these conflicting state and national in-

terests is realization that by its very nature the problem is incapable of precise and arithmetical solution. * * *

"* * * In a matter where exactness is concededly unobtainable and the feel of judgment so important a factor, we must be on guard lest unwittingly we displace the tax officials' judgment with our own."

Hence, it is not necessary that a state demonstrate its use of the single-factor formula has resulted in an exact measure of value. However, when a taxpayer comes forward with strong evidence tending to prove the formula employed will yield a grossly distorted result in its particular case, the state is obliged to counter that evidence to make the accommodation necessary to assure that its taxing power is confined to its constitutional limits. Norfolk & W. Ry. Co. v. Missouri State Tax Com'n, 390 U.S. 317, 329, 88 S.Ct. 995, 1003, 19 L.Ed.2d 1201, 1210.

In Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell, 283 U.S. 123, 135, 51 S.Ct. 385, ..., 75 L.Ed. 879, 908, the Court upset the application of a state apportionment formula upon a showing by the taxpayer that the percentage of income attributable to the taxing state was in fact "out of all appropriate proportion to the business transacted" by the taxpayer in the taxing state.

It appears to be well settled that a corporation doing business in several states challenging a formula of apportionment of income has the heavy burden of proving by "clear and cogent evidence" that the apportionment is grossly and flagrantly excessive. In support, see Norfolk & W. Ry. Co. v. State of North Carolina, 297 U.S. 682, 688, 56 S.Ct. 625, 628, 80 L.Ed. 977, 982.

Although, as stated, the trial court's ruling the Iowa single-sales-factor formula was facially unconstitutional in violation of due process is based upon the provisions

of both the federal and Iowa Constitutions, a separate discussion of the two constitutional provisions is not necessary under the general principle that similar constitutional guarantees are usually deemed to be identical in scope, import and purpose. Davenport Water Co. v. Iowa State Commerce Com'n, 190 N.W.2d 583, 593 (Iowa 1971).

Initially, the Director's contention the district court actually concluded section 422.33(1)(b) was violative of due process as applied, rather than on its face, can be disposed of summarily. It is true, as the Director contends, that in reaching its determination the district court refered to the stipulated factual circumstances present herein. However, reference to those facts was for the purpose of explaining the general operation of the statute in order to assess its facial validity. The Director's claim the trial court's analysis was inconsistent with its conclusion is without merit.

In reaching the conclusion section 422.33(1)(b), on its face, contravened principles of due process, the district court made the following analysis:

"In subjecting Moorman's arguments to due process scrutiny the initial inquiry must be whether 'the taxing power exerted by the state bears a relation to protection, opportunities and benefits given by the state. The simple, but controlling question is whether the state has given anything for which it can ask return.' State of Wisconsin v. J. C. Penney Co., 311 U.S. 435, 444 (1940) [61 S.Ct. 246, 250, 85 L.Ed. 267, 270-271, 130 A.L.R. 1229, 1233]. * * *

"Of course, Moorman, first and foremost, is accorded the not invaluable right to do business in the State of Iowa. The record shows its sales in Iowa are substantial. It is given the protection of Iowa laws with resort to the Iowa court system * * *. It is certain that Moorman's business

presence and activities in Iowa with this State's consent constitute the 'minimum connection' by which Iowa can constitutionally levy a corporate tax.

"The more narrow question presented, however, acknowledging that '. . . the tax * * * has relation to opportunities, benefits (and) protection conferred or afforded by (Iowa is whether) the tax is fairly apportioned to the commerce carried on within (this State). Norfolk & Western Railway Co. v. Missouri State Tax Commission, 390 U.S. 317, 325 (1968) (fn 5) [88 S.Ct. 995, 1001, 19 L.Ed.2d 1201].

"Said further by the *Norfolk & Western Railway* Court, * * * '* * * The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due. A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to "project the taxing power of the state plainly beyond its borders." (cited cases) Any formula used must bear a rational relationship, both on its face and in its application, to property values connected with the taxing State.'

"* * *

"While accepting the right of Iowa to tax its corporate income for the services, this State renders, it [Moorman] maintains that Iowa cannot tax *all* of Moorman's income, because only a small proportion of servicing inputs arise from its relation with this State. Since the largest quantum of capital and labor respecting its product sold here results from its Illinois relationship, the Iowa apportionment formula fails to reasonably apportion profits traceable to Illinois operations and taxes those

activities occurring in Illinois. In this sense, says Moorman, the single sales factor taxes more than that which should be fairly apportioned to Iowa and, as a consequence, violates its constitutional rights of due process * * *.

"We agree."

In support of its conclusion the district court relied heavily upon statements of the Court in General Motors Corp v. District of Columbia, 380 U.S. 553, 85 S.Ct. 1156, 14 L.Ed.2d 68.

In support of the trial court's ruling Moorman contends the Iowa single-sales-factor formula is facially unconstitutional in violation of due process of law because the formula attempts to tax *all* of the profits arising from sales of tangible personal property in Iowa even though the product is manufactured outside this state; thus, the single-sales-factor formula takes no cognizance of the contribution which the creation of the product outside the state makes to the realization of profit.

Moorman also asserts the Iowa single-sales-factor formula is facially unconstitutional in violation of the commerce clause of the United States Constitution because the formula does not fairly apportion net income to Iowa, causes multiple taxation of corporate net income by two or more states, and provides Iowa corporate businesses with direct commercial advantage not enjoyed by non-Iowa interstate business.

The sum of Moorman's argument is that the Iowa single-sales-factor formula is without economic or legal justification.

The Director, on the other hand, insists the formula provided in section 422.33(1) imposes a tax only on the

portion of net income reasonably attributable to the trade or business within Iowa.

At this point, it should be noted the Director's contention the same "test" is applicable with respect to both a constitutional challenge to the apportionment formula established by section 422.33(1)(b), based upon due process and a similar challenge founded upon the provisions of the commerce clause has some merit. However, while similar considerations are involved in the two constitutional determinations, it would be an overstatement to say they are identical. Notwithstanding some overlap, they will be dealt with separately herein. See Standard Pressed Steel Co. v. Washington Dept. of Rev., 419 U.S. 560, 95 S.Ct. 706, 42 L.Ed.2d 719.

In support of the contention the district court erroneously concluded section 422.33(1)(b) facially contravened due process guarantees, the Director asserts that the United States Supreme Court has never so held, and in fact, has consistently upheld single-factor apportionment formulae. He maintains the taxpayers in those cases which upheld single-factor formulae posited constitutional arguments identical to those asserted by Moorman to no avail, notwithstanding the fact that the tax schemes involved therein were much more harsh than Iowa's corporate tax scheme. Consequently, the Director maintains Moorman's allegations and the district court's determination are untenable.

In State of Wisconsin v. J. C. Penney Co., supra, 311 U.S. at 444, 61 S.Ct. at 249-250, 85 L.Ed. at ....., 130 A.L.R. at 1232-1233, is the following:

"The Constitution is not a formulary. It does not demand of states strict observance of rigid categories nor precision of technical phrasing in their exercise of the most

basic power of government, that of taxation. For constitutional purposes the decisive issue turns on the operating incidence of a challenged tax. A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society."

The Director relies heavily upon the sentiments expressed in the above opinion and upon a number of cases of the Supreme Court which approve single-factor apportionment formulae. See Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 41 S.Ct. 45, 65 L.Ed. 165; Bass, Ratcliff & Gretton v. State Tax Commission, 266 U.S. 271, 45 S.Ct. 82, 69 L.Ed. 282; National Leather Co. v. Massachusetts, 277 U.S. 413, 48 S.Ct. 534, 72 L.Ed. 935; Ford Motor Co. v. Beauchamp, 308 U.S. 331, 60 S.Ct. 273, 84 L.Ed. 304; Kent-Coffey Manufacturing Company v. Maxwell, 204 N.C. 365, 168 S.E. 397, 90 A.L.R. 476, aff'd., 291 U.S. 642, 54 S.Ct. 437, 78 L.Ed. 1040. It cannot be denied these cases are in fact supportive of the Director's contentions.

The Court has emphasized two points in evaluating the contention under the due process clause that an apportionment formula attributes more property or income to a taxing state than it may rightly claim. First, the Court has recognized that the very nature of the undertaking—the resort to a mathematical formula to determine the state's share of a business entity's tax base where there is no satisfactory way of determining it directly—involves rough approximation; and the Court has repeatedly held that the due process clause requires nothing more exacting. Second, the Court has made it plain that a taxpayer challenging an apportionment formula has more than the usual

heavy burden of proving by clear and convincing evidence that the application to it of the formula produces a grossly disproportionate result. Another basic principle which has emerged from the opinions of the Supreme Court recognizes that states are given the utmost leeway both in their choice and application of formulae for apportioning the net income of a corporation whose trade or business is carried on partly within and partly without its borders as long as basic considerations of due process and equal protection are observed.

The foregoing statements constitute a fair summary of the decisions of the Court in the cited cases.

With these principles in mind it is argued that in order to sustain the trial court's holding the apportionment formula prescribed in section 422.33(1) is "facially unconstitutional" this court would be required to conclude such a formula by its very terms will necessarily produce a "grossly distorted result" or an apportionment "out of all proportion to the business transacted."

We examine this contention in light of General Motors Corp. v. District of Columbia, 380 U.S. 553, 85 S.Ct. 1156, 14 L.Ed.2d 68, which was relied upon by the trial court in reaching its conclusion and by Moorman in its effort to support the trial court's ruling.

In the cited case the Court was faced with constitutional and statutory challenges to the method of apportionment utilized to determine tax liability under a franchise tax exacted by the District of Columbia. The statute in question provided for taxation on that portion of a corporation's net income which was "fairly attributable" to its activities within the District and authorized the tax commissioner to prescribe regulations concerning the appropriate apportionment formula to be used. General Motors

challenged the sales-factor formula on the ground it attributed to the District an unreasonably high proportion of its total income, and consequently, was contrary to the provisions of the enabling statute and violative of the due process and commerce clauses of the federal constitution.

The Court determined the sales-factor formula was contrary to the statute which authorized the collection of said tax and thus reversed the lower court "without reaching the constitutional questions raised." 380 U.S. at 555, 85 S.Ct. at 1158, 14 L.Ed.2d at ____.

We quote from the opinion:

"The conclusion which we reach by analysis of the plain language of the statute also finds support in the consequences which a contrary view would have for the overall pattern of taxation of income derived from interstate commerce. The great majority of States imposing corporate income taxes apportion the total income of a corporation by application of a three-factor formula which gives equal weight to the geographical distribution of plant, payroll, and sales. The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves. Conversely, in some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in the three-factor jurisdictions so that only 33% of their incomes will be subject to state taxation. * * *

"Moreover, the result reached in this case is consistent with the concern which the Court has shown that state taxes imposed on income from interstate commerce be fairly apportioned. In upholding taxes imposed on corporate income by Connecticut and New York and apportioned in accordance with the geographical distribution of a corporation's property, this Court carefully inquired into the reasonableness of the apportionment formulae used.

" 'The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut and ending with sale in other states. In this it was typical of a large part of the manufacturing business conducted in the state. The Legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. * * * There is * * * nothing in this record to show that the method of apportionment adopted by the state was inherently arbitrary, or that its application to this corporation produced an unreasonable result.' Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 120-121, 41 S.Ct. 45, 47, 65 L.Ed. 165. See also Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n, * * * [supra]. While the Court has refrained from attempting to define any single appropriate method of apportionment, it has sought to ensure that the methods used display a modicum of reasonable relation to corporate activities within the State. The Court has approved formulae based on the geographical distribution of corporate property and those based on the standard three-factor formula. * * * [citing authorities]. The standard three-factor formula can be justified as a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates. By contrast, the geogra-

phical distribution of a corporation's sales is, by itself, of dubious significance in indicating the locus of either factor. We of course do not mean to take any position on the constitutionality of a state income tax based on the sales factor alone. For the present purpose, it is sufficient to note that the factors alluded to by this Court in justifying apportionment measures constitutionally challenged in the past lend little support to the use of an exclusively sales oriented approach. In construing the District Code to prohibit the use of a sales-factor formula, we sacrifice none of the values which our scrutiny of state apportionment measures has sought to protect." 380 U.S. at 559-561, 85 S.Ct. at 1160-1161, 14 L.Ed.2d at .....

Although the Court in *General Motors* by way of dictum criticized the single-sales-factor apportionment formula it "refrained from attempting to define any single appropriate method of apportionment," and explicitly pointed out that its decision was not based on constitutional grounds when it said, "We of course do not mean to take any position on the constitutionality of a state's income tax based on the sales factor alone."

We have recognized the principle that courts have a duty to avoid constitutional questions when merits of a case may be fairly decided without facing such questions.

In Collier v. Denato, 247 N.W.2d 236, 241 (Iowa 1976), we quoted with approval this statement from State v. Thomas, 219 N.W.2d 3, 4 (Iowa 1974):

"* * * We prefer to decide cases on nonconstitutional grounds when possible. City of Des Moines v. Lohner, 168 N.W.2d 779, 782 (Iowa) ('We do not consider constitutional questions unless it is necessary for the disposition of the case.'); 16 Am.Jur.2d Constitutional Law § 113 at 301; 16 C.J.S. Constitutional Law § 94 at 317 ('The principle that

necessity of determination is a condition to judicial consideration of constitutional questions also finds application in the rule that such questons will not be passed on where the issues involved in the particular case may be decided on another ground, even though the constitutional issue has been properly presented.') * * *."

The same principle is announced in Alma Motor Co. v. Timken-Detroit Axle Co., 329 U.S. 129, 136, 67 S.Ct. 231, 234, 91 L.Ed. 128, 133 and authorities cited in footnote 8. See also Kovacs v. Brewer, 356 U.S. 604, 607, 78 S.Ct. 963, 966, 2 L.Ed.2d 1008, ...

Nevertheless, where the Court has employed the principle of avoidance of constitutional issues language used in such a decision does not afford a satisfactory basis for determining a state statute unconstitutional on its face. This is particularly true in light of the well-settled principles set out in division I hereof which this court adheres to in dealing with questions of a statute's constitutionality.

As noted, the burden is on the attacking taxpayer to demonstrate beyond a reasonable doubt that the act challenged here is unconstitutional on its face. There is nothing inconsistent with this principle and that announced in Butler Brothers v. McColgan, 315 U.S. at 507, 62 S.Ct. at 704, 86 L.Ed. at 996, that one who attacks a formula of apportionment of income of a corporation doing business in several states carries the distinct burden of showing by "clear and cogent evidence" that it results in extra-territorial values being taxed by the taxing state. The phrase "beyond a reasonable doubt" refers to the quantum of evidence necessary to sustain the attacking party's challenge on constitutional grounds, whereas the phrase "clear and cogent evidence" refers to the quality of evidence which must be offered by such party in an effort to sustain his burden of proof as to application of the formula issue.

There is another reason why we feel the *General Motors* decision is not determinative of the question considered in this division. As counsel points out, the statutory language on which decision turned in *General Motors* was not the provision making "net income * * * as is fairly attributable" to the District taxable; rather it was the specific requirement that net income derived from a trade or business carried on within and without the District shall "be deemed to be income from sources within and without the District." It was the Court's interpretation of this statutory phrase—which has no analogue in the Iowa statute and can scarcely be found in the due process clause—which was the fulcrum of the Court decision.

A search of the citator discloses General Motors Corp. v. District of Columbia has been cited in State Loan and Finance Corp. v. District of Columbia, 381 F.2d 895, 902 (D.C. Cir. 1967), on a proposition not involved here. We are unaware of any decision, federal or state, where it has been cited on the issue before us.

As noted, in its opinions in this area the Supreme Court has recognized: (1) the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as the unitary business under consideration here; (2) rough approximation rather than mathematical precision is sufficient; (3) the heavy burden cast upon the taxpayer in challenging a legislative enactment on constitutional grounds; and (4) the utmost leeway must be given the states both in their choice and application of formulae in this connection as long as basic considerations of due process and equal protection are observed.

In light of those principles we conclude section 422.33(1) calls for a method of allocation which is fairly calculated to assign to Iowa only that portion of the taxpayer's net income reasonably attributable to the trade or business done in Iowa since the taxing power exerted by this statute bears fiscal relation to the protection, opportunities and benefits given by the state. See Complete Auto Transit, Inc. v. Brady, ____ U.S. ____, 97 S.Ct. 1076, 1083, ____ L.Ed.2d ____. It is settled law that a state which provides an orderly market in which to transact business confers benefits which constitutionally justify the levy of an income tax. State of Wisconsin v. J. C. Penney Co., 311 U.S. 435, 61 S.Ct. 246, 85 L.Ed. 267.

It cannot logically be maintained that the apportionment formula prescribed by section 422.33(1) with the adjustments provided for in section 422.35 will necessarily produce a "grossly distorted result" or an apportionment "out of all proportion to the business transacted" in every conceivable situation which might possibly arise.

Thus far we have referred to only one of the fiscal years in issue—1968—in stating the percentage produced by application of the single-factor formula—22.617. The summary of exhibits 15 and 16 in Moorman's brief and argument shows application of this formula produced a percentage of 21.21 for 1969, 19.95 for 1970, 18.95 for 1971, and 18.67 for 1972.

Moorman points out employment of the three-factor formula would have resulted in a lower percentage for use in computing its income from sale of tangible personal property attributable to Iowa in those years.

However, the mere fact application of the single-factor formula results in a larger percentage being used for ascertaining the Iowa portion of the corporation's net income than would application of some other type of formula does not render the apportionment provision of the Iowa corporate income tax law facially unconstitutional

in violation of due process clauses of the federal and state constitutions. Such evidence alone does not establish that the difference between the two figures represents either double taxation or a taxation of extraterritorial values. Fairness is not equated with absolute precision.

In our opinion the formula in question meets the due process requirement of attempting to fairly allocate the corporation's income. In support of this conclusion see General Motors Corporation v. State, 181 Colo. at ____, 509 P.2d at 1266, and authorities cited.

The statute is free from the constitutional infirmities asserted and considered in this division. The trial court erred in holding otherwise.

III. The district court determined section 422.33(1)(b), on its face, contravened the principles embodied in the commerce clause of the federal constitution. The Director maintains such determination is erroneous as a matter of law.

The Director, perhaps overstating the similarity between the two constitutional analyses, does not distinguish between his due process and commerce clause contentions. The authorities and arguments posited in support of the former are likewise offered as supportive of the latter.

The considerations applicable to the resolution of a due process challenge to an apportionment formula are substantially similar to those utilized in assessing the validity of that formula with respect to the commerce clause. Extraterritorial taxation is constitutionally defective "both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due." Norfolk & W. Ry. Co. v. Missouri State Tax Com'n, supra, 390 U.S. at 325, 88 S.Ct. at 1001, 19 L. Ed.2d at ____.

The commerce clause prohibits a state from exacting a tax from an interstate corporation which is determined through application of inappropriate apportionment formulae, and consequently, subjects interstate commerce to the risk of multiple taxation. J. D. Adams Mfg. Co. v. Storen, 304 U.S. 307, 311-312, 58 S.Ct. 913, 916, 82 L.Ed. 1365; Gwin, White & Prince v. Henneford, 305 U.S. 434, 438-440, 59 S.Ct. 325, 327-328, 83 L.Ed. 272; Central Railroad Co. v. Commonwealth of Pa., 370 U.S. 607, 612, 82 S.Ct. 1297, 1301, 8 L.Ed.2d 720; Standard Pressed Steel Co. v. Washington Dept. of Rev., supra, 419 U.S. at 563-564, 95 S.Ct. at 709, 42 L.Ed.2d at ____. As a result of said multiple taxation, interstate commerce is put at a commercial disadvantage with respect to its local counterpart.

Moorman, relying upon the first paragraph of that portion of the General Motors Corp. v. District of Columbia opinion set out in division II, contends the apportionment formula prescribed by section 422.33(1)(b) results in multiple taxation of interstate commerce and a consequent, illegitimate benefit to Iowa manufacturers. Specifically, it maintains the sales-factor apportionment formula, on its face, subjects corporations manufacturing goods outside of Iowa and selling goods within this state to a tax on all income from their Iowa sales while the manufacturing states are also entitled to tax a portion of such income. In other words, Moorman assails the facial validity of 422.33(1)(b) on the ground it results in the taxation of more than 100% of a corporation's income from its Iowa sales. In addition, Moorman points out Iowa manufacturing corporations are not subject to such multiple taxation, and consequently, are the recipients of a statutorily based illegitimate commercial advantage.

Much of the analysis advanced in the previous division is of assistance in the resolution of Moorman's com-

merce clause contentions. Again, Moorman must satisfy the heavy burden of demonstrating that section 422.33(1)(b) violates the constitutional precept invoked. Furthermore, the weighty presumption of constitutionality is again operative.

Moorman's contention a foreign manufacturing corporation selling its products in Iowa is subject to tax on 100% of its income from Iowa sales ignores the provisions and application of section 422.35. That statutory provision provides for the adjustments necessary to arrive at a corporation's net income for Iowa tax purposes. A number of potentially large deductions are provided for therein, including the previously mentioned deduction of 50% of the federal tax liability incurred. Clearly, a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales. Consequently, Moorman has not demonstrated that the provisions of section 422.33(1)(b) result in a foreign corporation being taxed on more than 100% of its income from Iowa sales.

We rely again on the principles recognized by the Supreme Court in its opinions in this area as summarized in division II in concluding use of the single-sales-factor formula provided by the statute does not violate the commerce clause of the United States Constitution. The trial court erred in holding otherwise.

IV. On its cross appeal, Moorman maintains the district court erred as a matter of law in concluding section 422.33(1)(b), on its face, did not violate the guarantees of equal protection provided in the federal and state constitutions.

The district court ruled as follows with respect to Moorman's equal protection contentions:

"It is readily apparent that the statute in question focuses on the classification of 'corporations.' Since classifying corporations for different tax treatment than individual persons has most recently been sustained in Lehnhausen v. Lake Shore Auto Parts Co., 410 U.S. 356 (1973) [93 S.Ct. 1001, 35 L.Ed.2d 351], the Iowa scheme taxing corporations cannot be challenged merely because corporations are taxed. Nor does the fact that Section 422.33 establishes a graduated tax on corporate incomes lead to a finding of an invidious classification, for all corporations, without regard to any other factors, have been taxed by the same apportionment mechanism—the single sales factor. * * * [citing authority]. The simple matter is that for purposes of classification, the legislature has singled out the income for all 'corporations' as the basis on which the single sales factor is to apply; and while application of the formula yields differing amounts of tax due, for equal protection analysis, all corporations are similarly situated and are accorded exactly the same tax statement.

"This Court concludes that Iowa Code Section 422.33 on its face creates no classifications which may be found to violate Moorman's rights to equal protection of the law * * *. Indeed, Moorman's complaints concerning the operation of Section 422.33 would seem to be complaints shared by all corporations taxed by the statute whose operations are multi-state * * *."

Although Moorman argues section 422.33(1)(b) is facially invalid, its brief on cross appeal contains the following:

*"On its face, it would appear * * * section 422.33(1) does operate uniformly* upon all corporations engaged in the manufacture or sale of tangible personal property in the State of Iowa * * *.

"In fact, however, it is readily apparent that *the statute does not have a uniform operation.* * * *." (Emphasis deleted and supplied).

The quoted statements from Moorman's brief and the tenor of its contentions clearly demonstrate Moorman is in fact challenging the *application* of section 422.33(1)(b) to the particular circumstances herein. The authorities cited and arguments asserted will therefore be considered when Moorman's equal protection challenge to the sales-factor formula as applied to Moorman is considered in the next division.

In any event, even if Moorman is in fact attempting to challenge the facial validity of section 422.33(1)(b) with respect to equal protection guarantees, the contention is without merit. See City of New Orleans v. Dukes, ... U.S. ....., ..., 96 S.Ct. 2513, 2518, ... L.Ed.2d ....., ...

In Dickinson v. Porter, 240 Iowa 393, 400-401, 35 N.W. 2d 66, 72, are the following pertinent comments:

"If there is any reasonable ground for the classifications in this law and it operates equally upon all within the same class, there is uniformity in the constitutional sense and no violation of any constitutional provision invoked by plaintiff. * * * [citing authorities].

"The statute amounts to a legislative finding there are sufficient differences between property to which the act applies and other property to justify the classification. We will not interfere unless plaintiff has proven the classification does not rest on a reasonable basis but is essentially arbitrary and palpably discriminating. * * * [citing authority].

"It is well recognized the legislature has a wide discretion in determining classifications to which its acts shall

apply. * * * [citing authority]. In tax matters even more than in other fields, legislatures possess the greatest freedom in classification. * * * [citing authorities].

"It is not sufficient that the court may regard the reason for the classification a poor one. * * * [citing authorities]. The differences upon which the classification is based need not be great or conspicuous. * * * [citing authorities].

" 'An iron rule of equal taxation' is neither attainable nor necessary. * * * [citing authorities]."

Moorman's only attempt to demonstrate the unreasonableness of the classification contained in section 422.33(1)(b) is with reference to admittedly "extreme" hypothetical situations. Such a tactic clearly does not establish the classification is unreasonable. To the extent Moorman's position is that its situation comes within one of the hypotheticals posited, the contention more appropriately deals with the validity of the statute as applied and will be considered hereinafter.

Moorman's contention section 422.33(1)(b), on its face, violates equal protection guarantees is without merit.

V. As pointed out, in view of its ultimate conclusion, the district court did not feel compelled to resolve issues presented by Moorman's contentions other than those concerning the facial constitutionality of section 422.33(1)(b).

However, since this court has determined that the single-sales-factor formula is not facially defective, Moorman's contention section 422.33(1)(b) is constitutionally deficient as applied to Moorman with respect to the due process, equal protection and commerce clauses must be dealt with.

Moorman maintains the constitutional arguments advanced for invalidating that portion of the statute on its face are equally pertinent to its claim for overturning on constitutional grounds the application of the Iowa single-sales-factor formula to its net income. Hence, it reasserts by reference the arguments previously posited in support of the facial attacks on this statute, relying again most heavily upon General Motors Corp. v. District of Columbia, supra.

This court has determined section 422.33(1)(b), on its face, is free from constitutional defect. From that determination it follows said statutory provision may generally be applied to corporate entities subject thereto without constitutional transgression. However, a statute may be constitutional with respect to some factual situations but constitutionally infirm with respect to others. Williams v. Illinois, 399 U.S. 235, 242, 90 S.Ct. 2018, 2023, 26 L.Ed.2d 586; Walker v. Johnson County, 209 N.W.2d 137, 140 (Iowa 1973); A. B. C. Distrib. Co., Inc. v. City & Cty. of San Francisco, 15 Cal.3d 566, 125 Cal. Rptr. 465, 542 P.2d 625, 628-629; 16 Am.Jur.2d, Constitutional Law, section 194; 16 C.J.S., Constitutional Law, section 71, pages 217-218.

At this point the following statement from State v. Richardson, 285 A.2d 842, 846 (Me. 1972), is apposite:

"* * * One who seeks to assert a particular conglomerate of circumstances in which the operation of the statute might be unconstitutional must prove such facts in an actual case to test the constitutionality of the statute, as applied, rather than to seek to invalidate it on its face by hypothesizing marginal situations in which the statute might be conceived to operate with unduly oppressive or unjustifiably arbitrary impact indicative of unconstitutionality. * * * [citing authority]."

Moorman as the challenging party has the burden to demonstrate that section 422.33(1)(b), already found to be generally constitutionally valid, violates the constitutional precepts invoked when applied to it because of special factual circumstances surrounding Moorman's claim for relief.

Under the record, Moorman has not carried its burden, since it has not demonstrated by the stipulated facts the Iowa single-sales-factor-apportionment formula constitutes an unreasonable and arbitrary application in Moorman's particular case. No unusual or special factual circumstances inherent in Moorman's corporate operations are shown to exist. All that is established by the record is that Moorman apparently functions in a manner not dissimilar from the typical unitary business organization. No evidentiary justification is provided for a conclusion Moorman is somehow different from those corporations legitimately subject to the provisions of section 422.33(1)(b). In the absence of such evidence Moorman has not made out a sufficient case for overturning on constitutional grounds the application of the Iowa single-sales-factor formula to its net income.

VI. Article VIII, section 12, of the Iowa Constitution is applicable to corporations and provides as follows:

"Subject to the provisions of this article, the General Assembly shall have power to amend or repeal all laws for the organization or creation of corporations, or granting of special or exclusive privileges or immunities, by a vote of two-thirds of each branch of the General Assembly; and *no exclusive privileges, except as in this article provided, shall ever be granted.*" (Emphasis supplied).

Moorman directs this court's attention to the parties' stipulation which demonstrates that one foreign manufac-

turing corporation was permitted to use an alternative apportionment formula during the years in question. This approval by the Director of a formula other than the sales-factor formula prescribed in section 422.33(1)(b), allegedly amounts to the unauthorized grant of an exclusive privilege in violation of the above constitutional provision.

Moorman's contention is without merit. It is clear from the language of the constitutional provision in question that it applies to legislative enactments. Consequently, it has no application to alleged improprieties on the part of the Director. However, this should not be understood as assigning unfettered discretion to the Director. The general principles embodied in the constitutional provision are well covered by various other constitutional guarantees which are applicable to the Director's conduct.

VII. Moorman's next contention focuses upon the Director's failure to permit Moorman to utilize an alternative apportionment formula. It is argued the Director's rejection of Moorman's request was arbitrary and capricious and contrary to the provisions of section 422.33(2) which provides:

"If any taxpayer believes that the method of allocation and apportionment hereinbefore prescribed, as administered by the director and applied to his business, has operated or will so operate as to subject him to taxation on a greater portion of his net income than is reasonably attributable to business or sources within the state, he shall be entitled to file with the director a statement of his objections and of such alternative method of allocation and apportionment as he believes to be proper under the circumstances * * *; and if the director shall conclude that the method of allocation and apportionment theretofore employed is in fact inapplicable and inequi-

table, the director shall redetermine the taxable income by such other method * * * as seems best calculated to assign to the state for taxation the portion of the income reasonably attributable to business and sources within the state, not exceeding, however, the amount which would be arrived at by application of the statutory rules for apportionment."

The tenor of Moorman's argument concerning the Director's allegedly arbitrary and capricious conduct makes it impossible to separate this issue from the previous issues concerning the constitutionality of section 422.33(1)(b). Moorman's argument herein is based upon the constitutional invalidity of the sales-factor apportionment formula and, once again, relies almost exclusively upon General Motors Corp. v. District of Columbia, supra.

By reason of the determinations made in the previous divisions of this opinion we conclude Moorman's contention considered in this division is without merit.

The decisions reached in divisions II, III and IV of this opinion require a reversal upon the Director's appeal. By reason of the determinations reached in divisions V, VI and VII the matter is affirmed on Moorman's cross appeal.

All Justices concur except McCormick, J., who concurs specially.

McCORMICK, J. (concurring specially).

The United States Supreme Court has not yet decided the constitutionality of a corporate income tax formula which apportions net income of a unitary corporation based solely on the geographical distribution of sales. Although the Court has said "the geographic distribution of a corporation's sales is, by itself, of dubious significance in

indicating the locus [of either a corporation's sources of income or the social costs which it generates]," it has expressly refrained from taking "any position on the constitutionality of a state income tax based on the sales factor alone." However, the Court has noted "the factors alluded to by this Court in justifying apportionment measures challenged in the past lend little support to the use of an exclusively sales-oriented approach." General Motors Corporation v. District of Columbia, 380 U.S. 553, 561, 85 S.Ct. 1156, 1161, 14 L.Ed.2d 68, 73-74 (1965). In view of these statements by the Supreme Court in its most recent case touching on the subject, it seems reasonable to conclude that the constitutionality of Iowa's apportionment formula is open to question.

Moreover, I do not believe the *General Motors* case is wholly distinguishable on the basis suggested by the majority. Nevertheless, I agree with the majority that the case is not dispositive of the constitutional issues we face in this case. Further, under existing precedent of the Supreme Court and this court, I agree that Moorman did not establish the unconstitutionality of the Iowa apportionment formula either on its face or as applied here under the state due process clause and the federal due process and commerce clauses. Finally, I do not agree with the Director's view of his duty under Code § 422.33(2) but do not believe he breached his duty under the present record.

I. The problem addressed by the Court in *General Motors* was one of statutory interpretation. Hence the case did not involve principles of constitutional adjudication which implicate not only the heavy burden which must be met in demonstrating invalidity of a statute but also the distinction between invalidity of a statute on its face and as applied. See United States v. Raines, 362 U.S. 17,

80 S.Ct. 519, 4 L.Ed.2d 524 (1960). A statute is not unconstitutional on its face unless it is unconstitutional in every conceivable state of facts; it is ordinarily not unconstitutional as applied unless it is unconstitutional as applied in the specific factual situation before the court. The significance of this distinction is reflected in the position of the dissenters in *General Motors* in the court of appeals. They did not dispute the constitutionality of the single-factor formula on its face. See District of Columbia v. General Motors Corporation, 336 F.2d 885, 902-904 (D.C. Cir. 1964); see also Smoot Sand and Gravel Corp. v. District of Columbia, 261 F.2d 758, 763 (D.C. Cir. 1958) (" 'And the gross receipts formula has been in operation too long and upheld in the courts too frequently to be attacked as unfair or unreasonable *per se* or in the abstract.' "). To be unconstitutional on its face the formula would have to be unconstitutional all of the time, not just some of the time.

In *General Motors*, the Supreme Court based its decision on resolution of the issue whether the district tax commissioners acted within their statutory authority when they adopted a single-factor sales formula to determine the portion of corporate net income subject to the franchise tax. Two statutory directives existed. One required that the tax be on the portion of net income " 'fairly attributable to any trade or business carried on or engaged in within the District * * *.' " The other provided that the net income derived from the trade or business of any corporation " 'carried on or engaged in both within and without the District * * * be deemed to be income from sources within and without the District.' " *General Motors*, supra, 380 U.S. at 554-555, 85 S.Ct. at 1157, 14 L.Ed.2d at 70. In holding that the single-factor formula was inconsistent with these statutory directives, the Court relied on the fact that the formula would not apportion income to

non-sales income-producing activities outside the District. By statutory mandate, net income from District sales had to be considered the product in part of outside sources. Yet the sales factor formula would not apportion any income outside the District if all sales were made in the District, even though manufacturing occurred elsewhere.

I do not believe the existence of the second statutory requirement wholly distinguishes *General Motors* from the present case on the theory this directive is not part of the constitutional standard. Of course, the first statutory requirement is identical to the constitutional mandate under the due process and commerce clauses that a tax be fairly apportioned to commerce carried on within the taxing jurisdiction. See Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450, 79 S.Ct. 357, 3 L.Ed.2d 421 (1959); Annot., 34 L.Ed.2d 749, 765. I believe the second requirement is part of the constitutional standard when non-sales income-producing activities do occur outside the taxing jurisdiction. For example, when manufacturing activity occurs outside the jurisdiction, I believe profit realized upon sale of the manufactured goods in the taxing jurisdiction must be deemed to arise from that activity as well as from the sale. This is as basic as the principle of contradictions. A stick cannot have only one end. Similarly, income cannot be isolated from the capital or labor, or both, which produce the product or service which is sold. This is a matter of self-evident fact rather than a matter of "economic theory" as suggested by the Director in this case.

This fact has been consistently recognized by the Supreme Court. See Stratton's Independence v. Howbert, 231 U.S. 399, 34 S.Ct. 136, 58 L.Ed. 285 (1913). It is basic to the apportionment formula cases. In Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 120, 41 S.Ct. 45, 47,

65 L.Ed. 165, 169 (1920), the Court observed, "The profits of the corporation were largely earned by a series of transactions *beginning with manufacture in Connecticut and ending with sale in other States.* (emphasis added). The challenge to the apportionment formula failed in *Underwood* because the taxpayer failed to demonstrate the apportionment formula, based on the geographical situs of real and tangible personal property, reached more than the profits actually earned by the income-producing activities in the taxing state. A different result occurred in Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell, 283 U.S. 123, 51 S.Ct. 385, 75 L.Ed. 879 (1931), precisely because the taxpayer did meet that burden. ("[T]he statutory method, as applied to the appellant's business for the years in question, operated unreasonably and arbitrarily in attributing to North Carolina a percentage of income out of all appropriate proportion to the business transacted by the appellant in that state.") 283 U.S. at 135, 51 S.Ct. at 389, 75 L.Ed. at 908. The constitutional standard is premised on the theory that each transaction from manufacture through sale contributes to the income which is realized, but it puts the heavy burden on the taxpayer to demonstrate what share of his income from a unitary corporation is attributable to activities in the taxing jurisdiction, and further, that the apportionment formula produces a grossly distorted result in those circumstances. *Id.*, 283 U.S. at 133, 51 S.Ct. at 389, 75 L.Ed. at 905 ("The difficulty of making an exact apportionment is apparent and hence, when the state has adopted a method not intrinsically arbitrary, it will be sustained until proof is offered of an unreasonable and arbitrary application in particular cases.").

Any single-factor formula is thus capable of producing a grossly distorted result because it focuses artificially on only one component of the corporation's income-produc-

ing activities. See, e.g., Norfolk and Western Railway Company v. Missouri State Tax Commission, 390 U.S. 317, 88 S.Ct. 995, 19 L.Ed.2d 1201 (1968). Less danger exists that a multiple-factor formula will have that result because it recognizes additional relevant components.

I believe the Supreme Court struck the single-factor sales formula in *General Motors* because it read the governing statute as requiring adoption by the commissioners of an apportionment formula which would never deny recognition to non-sales income-producing activities which occurred outside the District. The case is distinguishable from the present one because the constitutional standard does not demand as much. Instead, it prohibits use of an apportionment formula which, in a given case, grossly overstates the portion of net income attributable to income-producing activities in the taxing jurisdiction. While this standard makes a single-factor sales formula more susceptible to successful attack in a particular application—for example when all sales occur in the taxing jurisdiction and all manufacturing occurs in another jurisdiction—it does not make a single-factor sales formula unconstitutional in every conceivable circumstance nor does it relieve the taxpayer of his burden to prove unconstitutionality of its application.

In the present case, Moorman did not attempt to prove the amount of its actual net income from Iowa activities in the years involved. Therefore no basis was presented for comparison of the corporation's Iowa income and the income apportioned to Iowa under the formula. In this era of sophisticated accounting techniques, it should not be impossible for a unitary corporation to prove its actual income from activities in a particular state. However, Moorman showed only that its tax liability would be substantially less if Iowa employed a three-factor apportionment formula. We have no basis to assume that the three-factor formula produced a result equivalent to the corporation's actual income from Iowa activities. Having failed to establish a basis for comparison of its actual income in Iowa with the income apportioned to Iowa under the single-factor formula, Moorman did not demonstrate that the single-factor formula produced a grossly unfair result. Thus it did not prove unconstitutionality of the formula as applied.

II. We are not limited in our interpretation of the due process clause of Ia. Const. Art. I § 9 by interpretations of the same language in U.S. Const. Amend. 14 by the Supreme Court. Deference to federalism has led the Supreme Court to accord states wide latitude in economic matters. See New Orleans v. Dukes, 427 U.S. 297, 303, 96 S.Ct. 2513, 2516-2517, 49 L.Ed.2d 511, 516-517 (1976). This factor does not inhibit state courts applying similar state constitutional provisions. In addition, we have the independent right to say what our state constitution means. See Brennan, *State Constitutions and the Protection of Individual Rights,* 90 Harv. L. Rev. 489 (1977). However, the distinction makes no practical difference in the present case because we have accorded equivalent latitude to the legislature in tax matters under our state constitution. See City of Waterloo v. Selden, 251 N.W.2d 506 (Iowa 1977).

III. I do not believe Moorman's attack on the single-factor apportionment formula is answered by the Director's reliance on the frequent statement of the Supreme Court that, because of the practical impossibility of a state's achieving perfect apportionment, a "rough approximation" is sufficient. See International Harvester Co. v. Evatt, 329 U.S. 416, 67 S.Ct. 444, 447, 91 L.Ed. 390, 395 (1947). This rule does not excuse a state from trying to achieve

fairness, nor does it excuse a state from using a different formula in situations where it is demonstrated that an existing formula grossly overreaches.

IV. Similarly, I do not agree with the Director that his power to grant relief under Code § 422.33(2) is limited to situations where application of the sales factor formula would be unconstitutional. I do not understand that the majority opinion approves this interpretation, but does not pass on it. I would disapprove it. The statute does not purport to impose upon the taxpayer a burden of proving unconstitutionality in order to obtain relief from the formula. Instead, he is merely required to file a statement of his objections and set forth "such alternative method of allocation and apportionment as he believes to be proper under the circumstances * * *." In turn, the Director is not precluded from affording relief except when the taxpayer proves a grossly distorted result will ensue from use of the sales formula. Rather he is empowered to grant relief when he finds the statutory formula "inapplicable and inequitable." The statute vests the Director with reasonable administrative discretion and manifests a legislative intention that it be exercised. No issue is presented in this case regarding the constitutionality of this delegation of power.

I do not believe Moorman was prejudiced by the Director's refusal to exercise this discretion in the present case because the record does not show Moorman made an adequate case for its exercise.

I concur in the result.

IN THE SUPREME COURT OF IOWA

No. 2-60220

MOORMAN MANUFACTURING COMPANY,
Plaintiff-Appellee,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant-Appellant.

ORDER

(Filed June 27, 1977)

Plaintiff-Appellee's petition for rehearing in the above entitled matter has been duly considered by the entire membership of the court and is now refused and denied.

Done this 27th day of June, 1977.

/s/ C. Edwin Moore
Chief Justice—Iowa Supreme Court

Copies to:

Walter R. Brown
John V. Donnelley
1200 Register & Tribune Bldg.
Des Moines, Iowa 50309

Harry Griger
Assistant Attorney General

APPENDIX D

IN THE SUPREME COURT OF IOWA

No. 2-60220

MOORMAN MANUFACTURING COMPANY
Appellee,
v.
G. D. BAIR, DIRECTOR OF REVENUE
STATE OF IOWA
Appellant.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

(Filed August 4, 1977)

Notice is hereby given that Moorman Manufacturing Company, the Appellee above-named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of Iowa reversing the rulings of the Polk County District Court in favor of Appellee and affirming the District Court's rulings adverse to Appellee entered in this action on May 25, 1977 and from the denial of Appellee's Petition for Rehearing entered on June 27, 1977.

This appeal is taken pursuant to 28 U.S.C. §1257(2).

/s/ Walter R. Brown
Walter R. Brown

/s/ John V. Donnelly
John V. Donnelly
Swift, Brown and Winick
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Attorneys for Appellee

APPENDIX E-1

CONSTITUTION OF THE UNITED STATES

ARTICLE I.

• • •

Section 8. The Congress shall have Power . . .

• • •

To regulate Commerce . . . among the several States . . .;

AMENDMENT 14.

Section 1. • • •; nor shall any State deprive any person of . . . property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

APPENDIX E-2

CODE OF IOWA

422.33 Corporate tax imposed

A tax is hereby imposed upon each corporation organized under the laws of this state, and upon every foreign corporation doing business in this state, annually in an amount equivalent to four percent of the net income received by such corporation during the income year.

1. If the trade or business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income, but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on the portion of the net income reasonably attributable to the trade or business within the state, said net income attributable to the state to be determined as follows:

a. Interest, dividends, rents and royalties (less related expenses) received in connection with business in the state, shall be allocated to the state, and where received in connection with business outside the state, shall be allocated outside of the state.

b. Net income of the above class having been separately allocated and deducted as above provided, the remainder of the net income of the taxpayer shall be allocated and apportioned as follows:

* * *

Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

The gross sales of the corporation within the state shall be taken to be the gross sales from goods sold and delivered within the state, excluding deliveries for transportation out of the state.

For the purpose of this section, the word "sale" shall include exchange, and the word "manufacture" shall include the extraction and recovery of natural resources and all processes of fabricating and curing. The words "tangible personal property" shall be taken to mean corporeal personal property, such as machinery, tools, implements, goods, wares, and merchandise, and shall not be taken to mean money deposits in banks, shares of stock, bonds, notes, credits, or evidence of an interest in property and evidences of debt.

2. If any taxpayer believes that the method of allocation and apportionment hereinbefore prescribed, as administered by the commission and applied to his business, has operated or will so operate as to subject him to taxation on a greater portion of his net income than is reasonably attributable to business or sources within the state, he shall be entitled to file with the commission a statement of his objections and of such alternative method of allocation and apportionment as he believes to be proper under the circumstances with such detail and proof and within such time as the commission may reasonably prescribe; and if the commission shall conclude that the method of allocation and apportionment theretofore employed is in fact inapplicable and inequitable, it shall redetermine the taxable income by such other method of allocation and apportionment as seems best calculated to assign to the state for taxation the portion of the income reasonably attributable to business and sources within the state, not exceeding, however, the amount which would be arrived at by application of the statutory rules for apportionment.

(Note: The foregoing Section 422.33, Code of Iowa, is as it appears at Vol. II, p. 1669 of the 1966 edition of the Code; it has been amended subsequently in respects not material to this case and appears in its latest form in Code of Iowa (1977), Vol. II, p. 2078.)

422.35 Net income of corporation—how computed.

The term "net income" means the taxable income less the net operating loss deduction, both as properly computed for federal income tax purposes under the Internal Revenue Code of 1954, with the following adjustments:

1. Subtract interest and dividends from federal securities.

2. Add interest and dividends from foreign securities and from securities of state and other political subdivisions exempt from federal income tax under the Internal Revenue Code of 1954.

3. Where the net income includes capital gains or losses, or gains or losses from property other than capital assets, and such gains or losses have been determined by using a basis established prior to January 1, 1934, an adjustment may be made, under rules and regulations prescribed by the state tax commission, to reflect the difference resulting from the use of a basis of cost or January 1, 1934, fair market value, less depreciation allowed or allowable, whichever is higher. Provided that the basis shall be fair market value as of January 1, 1955, less depreciation allowed or allowable, in the case of property acquired prior to that date if use of a prior basis is declared to be invalid.

4. Subtract federal income taxes paid or accrued, as the case may be, during the tax year, adjusted by any

federal income tax refunds; and add the Iowa income tax deducted in computing said taxable income.

5. Add the amount by which the basis of qualified depreciable property is required to be increased for depreciation purposes under the Internal Revenue Code Amendments Act of 1964 to the extent that such amount equals the net amount of the special deduction allowed on the basis of the amount by which the depreciable basis of such qualified property was required to be reduced for depreciation purposes under the Internal Revenue Code Amendments Act of 1962. The "net amount of the special deduction" shall be computed by taking the sum of the amounts by which the basis of qualified property was required to be decreased for depreciation purposes for the years 1962 and 1963 and subtracting from it the sum of the amounts by which the basis of such property was required to be increased, prior to 1964, for depreciation or disposition purposes under the Internal Revenue Code Amendments Act of 1962.

Provided, however, that a corporation affected by the allocation provisions of section 422.33 shall be permitted to deduct only such portion of the deductions for net operating loss and federal income taxes as is fairly and equitably allocable to Iowa, under rules and regulations prescribed by the state tax commission.

(Note: The foregoing Section 422.35, Code of Iowa, is as it appears at Vol. II, p. 1670 of the 1966 edition of the Code; with respect to taxable years beginning on or after January 1, 1967, Subsection 4 was amended by inserting "fifty (50) per cent of the" preceding the words "federal income taxes", Acts of 1967 (62 G.A.) ch. 348, §17. The latest form of Section 422.35 appears in Code of Iowa (1977), Vol. II, p. 2080.)

MOTION FILED
SEP 22 1977

No. 77-454

IN THE
Supreme Court of the United States
OCTOBER TERM, 1977

MOORMAN MANUFACTURING COMPANY,
Appellant

v.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Appellee

On Appeal from the Supreme Court of the State of Iowa

MOTION OF WILLIAM J. BAUMOL, *ET AL.* FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE IN SUPPORT OF APPELLANT'S JURISDICTIONAL STATEMENT AND APPEAL

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IN THE

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OCTOBER TERM, 1977

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G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
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On Appeal from the Supreme Court of the State of Iowa

MOTION OF WILLIAM J. BAUMOL, *ET AL.* FOR LEAVE TO FILE BRIEF AMICUS CURIAE IN SUPPORT OF APPELLANT'S JURISDICTIONAL STATEMENT AND APPEAL

The individuals identified below hereby respectfully move for leave to file the attached brief *amicus curiae* in support of this appeal. The consent of the attorney for the Appellant has been obtained. The consent of the attorney for the Appellee was requested but refused. The Appellant's letter of consent and the Appellee's letter of refusal are submitted herewith.

The identities of the movants and brief statements of their qualifications are as follows:

WILLIAM J. BAUMOL, Professor of Economics, Princeton University and New York University; formerly Vice President, American Economic Association.

OSWALD H. BROWNLEE, Professor of Economics, University of Minnesota; formerly Deputy Assistant Secretary of the Treasury.

JAMES M. BUCHANAN, University Professor of Economics and Director, Center for the Study of Public Choice, Virginia Polytechnic Institute and State University; formerly President, Southern Economic Association; Vice President, American Economic Association.

COLIN D. CAMPBELL, Professor of Economics, Dartmouth College.

OTTO A. DAVIS, Professor of Political Economy and Dean of the School of Urban and Public Affairs, Carnegie-Mellon University.

MILTON FRIEDMAN, Paul Snowden Russell Distinguished Service Professor of Economics, University of Chicago; formerly President, American Economic Association; Alfred Nobel Memorial Prize in Economic Science (1976).

C. LOWELL HARRISS, Professor of Economics, Columbia University; formerly President, National Tax Association.

PAUL W. MACAVOY, Professor of Economics, Yale University; formerly member, President's Council of Economic Advisers.

HENRY G. MANNE, Distinguished Professor and Director, Law and Economics Center, School of Law, University of Miami.

WILLIAM H. MECKLING, Professor of Economics and Dean, College of Business Administration, University of Rochester.

DAVID I. MEISELMAN, Professor of Economics and Director, Reston Economics Program, Virginia Polytechnic Institute and State University; formerly Chairman, Presidential Task Force on Inflation.

MANCUR L. OLSON, Professor of Economics, University of Maryland; formerly Deputy Assistant Secretary, Department of Health, Education and Welfare.

RICHARD N. ROSETT, Professor of Business Economics and Dean, Graduate School of Business, University of Chicago.

LESTER C. THUROW, Professor of Management and Economics, Massachusetts Institute of Technology.

MURRAY L. WEIDENBAUM, Mallinckrodt Distinguished University Professor of Economics and Director, Center for the Study of American Business, Washington University, St. Louis; formerly Assistant Secretary of the Treasury for Economic Policy.

The interest of the movants in this case arises from the fact that, as academic economists of long and distinguished experience, they are greatly concerned that affirmance of the decision below, which held constitutional the apportionment of net income for Iowa tax purposes based upon the single factor of the place of sale, without regard for the place where capital and labor were employed in producing the income, will raise unacceptable barriers to interstate competition in the national common market and contravene a fundamental principle of federalism embodied in our Constitution.

When the same constitutional issue was previously before this Court, in *General Motors Corp.* v. *District of Columbia*, 380 U.S. 553 (1965), October 1964 Term No. 352, the record contained expert testimony concerning the economic effects of the use of the single factor formula based upon sales. Since the case was decided (against

the use of the single factor formula) on statutory rather than constitutional grounds, that testimony was not relied upon or referred to by the Court in reaching its decision, although its substance was thoroughly woven into the Court's reasoning. The present record does not contain comparable economic testimony, and the economic effects cannot as adequately be demonstrated merely by argument of counsel. Movants respectfully entreat the Court, therefore, to consider the economic effects, presented as argument by a distinguished panel of economists, based upon facts of which the Court may take judicial notice.

Respectfully submitted,

WILLIAM T. PLUMB, JR.
Attorney for the Amici Curiae

IN THE
Supreme Court of the United States
OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant

v.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Appellee

On Appeal from the Supreme Court of the State of Iowa

BRIEF AMICUS CURIAE SUBMITTED BY WILLIAM J. BAUMOL, *ET AL.* IN SUPPORT OF APPELLANT'S JURISDICTIONAL STATEMENT AND APPEAL

This brief is submitted by the following individuals in their personal capacities. Biographical information is included solely for purposes of identification, and no position is taken by any organization or institution mentioned in connection with the named intervenors.

Interstate competition, unhindered by state barriers to trade, is basic to the American federal system of government. This view has its most obvious origin—whether

it be called economic or political—in the United States Constitution. The principle has been reinforced repeatedly through two centuries of consistent holdings by this Court, as well as through such important economic legislation as the Sherman Anti-trust Act and other laws aimed at preserving competition. But the battle to preserve a national common market and free trade is an unending one, for in a dynamic federal system like ours, state regulations or taxes can have decidedly different economic impacts at different times and under different circumstances.

This point is well illustrated by the Iowa tax at issue in the instant proceedings. This tax, as will be shown, has under its existing circumstances, the anti-competitive effect that would seem to signify its unconstitutionality. And it is the effect on competition, not the form of a particular tax, to which the constitutional provision barring state interferences with interstate commerce must logically be related. It is also this market effect on competition, and not the structure of the Iowa tax as such, which gives rise to the belief of the amicus petitioners that their own interests, as well as those of all American consumers, are best served by constitutional preservation of the American common market.

One of the most important ways in which competition controls economic activity is to create pressures to eliminate higher cost producers. When these higher costs are due to inefficient management or inefficient production techniques, this pressure to eliminate certain firms or force them to perform more efficiently is unequivocally socially desirable. However, competition will have this excluding effect regardless of the particular cause of higher costs. Thus the effects of a differentially higher tax rate will be precisely the same on a firm in a competitive industry as will a poor management policy that "costs" the same amount. But in the tax case com-

petition is actually prevented from performing the socially useful function of eliminating undesirable economic inefficiencies. And this is exactly the effect of the Iowa "single-factor" tax formula when adopted in the face of the otherwise universal use of a three-factor attribution test.

The application by Iowa of a corporate income tax based on the single-factor attribution of gross revenues necessarily increases the cost of doing business in Iowa of a foreign corporation compared to the cost of a competing domestic firm. The point can be easily illustrated by numerical examples using some arithmetically simplifying assumptions.

Suppose that two identical corporations, one domiciled in Iowa and one domiciled in Illinois, each have the same total sales equally divided between the two states. Suppose further that the total property and payroll of each corporation rests exclusively in the state in which it is domiciled, and that each corporation has a total income (taxable accounting profits) of $1 million. Finally, suppose that both Iowa and Illinois levy a 5 percent income tax. Now we consider the effects of applyng the tax using different tax formulas.

If Iowa and Illinois use a single-factor formula, that is, one levying the 5 percent tax exclusively on the basis of income attributable to the proportion of total sales made in each state, then the tax formula is:

$$\frac{\text{sales in a state}}{\text{total sales}} \text{ X total net income X } 0.05. \qquad (1)$$

We assume that each corporation has half of its sales in each state, and thus its tax payments to each state would be:

$$(0.50)\ (1{,}000{,}000)\ (0.05) = \$25{,}000 \qquad (2)$$

and the pattern of tax payments and receipts is that shown in Table 1:

TABLE 1

	Taxes Paid to Iowa	Taxes Paid to Illinois	Total Taxes Paid by each Corporation
Iowa Corp.	25,000	25,000	50,000
Illinois Corp.	25,000	25,000	50,000
TOTAL	50,000	50,000	

If both Iowa and Illinois again levy the same 5 percent income tax but use the traditional three-factor formula, which is:

$$\frac{\frac{\text{Sales in State}}{\text{Total Sales}} + \frac{\text{Property in State}}{\text{Total Property}} + \frac{\text{Payroll in State}}{\text{Total Payroll}}}{3} \times \text{Total net income} \times 0.05, \qquad (3)$$

then each corporation's payment to its state of domicile would be

$$\frac{0.5 + 1 + 1}{3} \times 1{,}000{,}000 \times 0.05 = 41{,}667, \text{ and} \qquad (4)$$

its payment to the state in which it is a foreign corporation would be

$$\frac{0.5 + 0 + 0}{3} \times 1{,}000{,}000 \times 0.05 = 8{,}333, \qquad (5)$$

and the pattern of tax payments and receipts would be that shown in Table 2:

TABLE 2

	Taxes Paid to Iowa	Taxes Paid to Illinois	Total Taxes Paid by each Corporation
Iowa Corp.	41,667	8,333	50,000
Illinois Corp.	8,333	41,667	50,000
TOTAL	50,000	50,000	

But now consider the basic situation at issue in the present case, in which Iowa uses the single-factor formula, whereas Illinois uses the three-factor formula. Utilizing the same data specified earlier, the pattern

of tax payments and receipts is now that shown in Table 3:

TABLE 3

	Taxes Paid to Iowa	Taxes Paid to Illinois	Total Taxes Paid by each Corporation
Iowa Corp.	25,000	8,333	33,333
Illinois Corp.	25,000	41,667	66,667
TOTAL	50,000	50,000	

Under the simplifying hypothetical conditions stated earlier, each state's tax receipts are the same ($50,000) in each tax situation. But, as Table 1, 2 & 3 demonstrate the corporations' tax payments will be the same only if both states use the same formula. If Iowa uses the single-factor method while Illinois uses the three-factor method, then, as shown in the last column of Table 3, the Iowa corporation pays exactly one-half the amount of total state income taxes ($33,333) paid by the Illinois corporation ($66,667).

In practice, of course, these relative differentials will be smaller or greater depending upon the actual tax rates levied by the various states involved, and upon the actual proportions of domestic to foreign sales, payrolls, and properties of individual corporations. Only the magnitudes will change with these factors, however, and not the direction of the impact. The general principle will apply in all cases.

As a result of Iowa's decision to apply a single-factor formula in the context of general use of the three-factor formula by other states, Iowa corporations will enjoy lower total state income tax payments than foreign corporations doing business in Iowa, and these foreign corporations will be burdened by higher payments to Iowa than would otherwise be true. The necessary effect of this situation is to improve the competitive position of Iowa corporations by increasing the costs of foreign competitors.

Several specific aspects of this analysis deserve emphasis. First, the constitutional right of Iowa to levy taxes of any particular rate is not here questioned. What is questioned is the choice of a tax formula that effectively discriminates in favor of domestic corporations at the expense of foreign corporations and thus lessens competition. That is the only effect that follows necessarily from Iowa's selection of the one factor attribution, since it cannot even be concluded a priori that Iowa's choice of a single-factor rather than a three-factor formula will yield higher receipts. That will depend, among other reasons, upon how these corporations respond to the tax. So we can logically conclude that if Iowa's objective is simply to increase its tax revenues, then it could simply raise its tax rate while applying the three-factor formula. That it does not pursue that strategy would seem to indicate that protection of domestic corporations rather than merely revenue considerations plays an important part in Iowa's decision to use a single-factor formula.

It should also be noted that the anti-competitive effect of this tax works in still another way. Many taxes are properly and logically justified on the basis of benefits provided to the taxpayer by the taxing authority. These include police and fire protection, courts, and numerous other amenities. To the extent that the instant Iowa tax receipts are utilized to provide such benefits, they will naturally disproportionately benefit Iowa corporations. While it is not suggested that this disparate effect is necessarily in and of itself constitutionally unsound, it does reinforce the position already discussed that the one factor attribution in a context of all other states using the three factor test does have undesirable anti-competitive effects. Here, however, the discrimination is on the side of the benefits rather than the costs, as Illinois corporations are taxed for service disproportionately benefiting their Iowa competitors.

As the political pressures build in one state and then another to secure these hidden competitive benefits for domestic businesses through selection of appropriate tax formulas, the specter of a severely damaging, yet not openly declared trade war between states begins to threaten. No conceivable economic advantage could justify the economic costs attendant upon such conflict.

As mentioned earlier, the tax paid to any and all states goes into the determination of the total cost of production for a given corporation. Clearly, to survive in the long run, all these costs must be recovered. But this cost recovery can only be accomplished ultimately by a sale of the goods produced. In this sense then revenue from sales includes recovery of labor and property costs wherever they may have been incurred, and therefore a gross revenue tax necessarily constitutes a tax on every component factor of production, regardless of where located.

Thus the Iowa tax based on sales revenue for an Illinois corporation producing in Illinois in effect becomes a tax on property and payrolls in Illinois. But these items are already being taxed in Illinois via the three factor formula. Therefore another economic effect of Iowa's one-factor formula is to let it tax labor and productive capital that is in no way physically associated with the State of Iowa. This is, of course, an alternative way of looking at the anti-competitive effect described earlier, and it is mentioned here primarily to demonstrate that the economic consequences of the Iowa formula may run afoul of more than one constitutional standard for an acceptable state tax.

A common market or free trade area encourages production to be undertaken by the least-cost producers regardless of their domicile. The organization of economic activity according to this principle benefits consumers by giving them a wider choice of goods and services at lower prices, and it rewards producers for more efficient, lower-

cost production. Society collectively benefits, since lower-cost production releases resources that can now find added use to increase the health and welfare of all members of society. Courts should be ever mindful of the threat states can pose to the effective workings of a free and open marketplace.

Regardless of the intention of the framers of the Iowa tax the effect is clearly contrary to the principle of federalism that underlies the Commerce Clause of the United States Constitution. The necessary effect of this tax is precisely the same as an Iowa tariff imposed on Illinois or other corporations doing business in Iowa in competition with Iowa companies. To allow this state of affairs to persist in any state is to invite, indeed even to force, retaliation by other states. It presents the quintessential situation in which the Supreme Court has the responsibility for preserving the Federal system in its economic component. It is a matter of utmost importance that this Court address itself once again to this issue and prevent the development of debilitating internal economic conflict in the United States.

Respectfully submitted,

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

v.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Appellee

MOTION OF MOTOR VEHICLE MANUFACTURERS ASSOCIATION OF THE UNITED STATES, INC., FOR LEAVE TO FILE BRIEF AS AMICUS CURIAE

and

BRIEF OF MOTOR VEHICLE MANUFACTURERS ASSOCIATION OF THE UNITED STATES, INC., AS AMICUS CURIAE

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STATE OF IOWA,
Appellee

MOTION OF MOTOR VEHICLE MANUFACTURERS ASSOCIATION OF THE UNITED STATES, INC., FOR LEAVE TO FILE BRIEF AS AMICUS CURIAE

Motor Vehicle Manufacturers Association of the United States, Inc. (the Association) respectfully moves this Court for leave to file the accompanying brief in this case as *amicus curiae*. The consent of the Appellant has been obtained, but the Appellee has refused his consent.

The applicant, a non-profit trade association whose members manufacture and sell motor vehicles in the United States, has an interest in this case in that several of its members are assessed and are contesting the Iowa income tax. The assessed tax on these members is not being paid pending a final decision of the instant case, because their liability depends on a determination of the questions which are presented for decision herein.

The Association believes that Appellant will be unable to develop fully economic data bearing on this case. The Associa-

tion wishes to present factual information relating to the impact of the challenged tax on the U.S. automobile industry. This information cannot be presented by Appellant, and it will be unknown to the Court unless presented by the Association as *amicus curiae*. It is desirable that the Court have these facts before it in considering Appellant's jurisdictional statement, because these facts demonstrate the broad scope of the issues and their importance both in Iowa and nationally.

Respectfully submitted,

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IN THE

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BRIEF OF MOTOR VEHICLE MANUFACTURERS ASSOCIATION OF THE UNITED STATES, INC., AS AMICUS CURIAE

INTEREST OF AMICUS CURIAE

Motor Vehicle Manufacturers Association of the United States, Inc. is a non-profit membership corporation organized under the laws of New York, and its members manufacture well over 90% of all passenger automobiles, trucks and busses produced in the United States. This brief is filed on behalf of the following members of the Association:

> American Motors Corporation, Checker Motors Corporation, Chrysler Corporation, Ford Motor Company, General Motors Corporation, International Harvester Company, PACCAR, Inc., Walter Motor Truck Company, and Warner & Swasey Company

All of these members are engaged in interstate commerce. None of these members has production or assembly facilities in the State of Iowa, but sales by these members through interstate commerce into Iowa in 1976 alone were in excess of $1,250,000,000. Several members are presently contesting the

Iowa apportionment formula and all such contesting members have offered to pay Iowa income tax based on formulae involving the three factors of property, payroll and sales.

In addition, various members of the Association pay corporate income taxes in the other 45 jurisdictions (44 states and the District of Columbia) imposing such taxes, and the Court, by considering this case, can instruct all such taxing units as to the constitutional boundaries of their fiscal powers, thereby eliminating the uncertainties created by the Iowa Supreme Court's ruling.

THE ISSUE

The issue in this case is whether the single-factor destination sales formula for the "apportionment" of net income of foreign corporations to Iowa prescribed by Sections 423.33 and 422.35 of the Code of Iowa violates the Commerce Clause (Art I, Sec 8, Cl 3) of the Constitution of the United States and the Due Process and Equal Protection Clauses of the Fourteenth Amendment thereto.

The Iowa supreme court sustained the single-factor sales formula as constitutional. The *amicus curiae* believes that the Iowa supreme court did not give proper consideration to the clear policy direction provided by this Court to avoid the multiple taxation resulting from application of a statutory formula such as Iowa's.

ARGUMENT

In *General Motors Corp.* v. *District of Columbia*, 380 U.S. 553, 561-562, this Court implemented its "continuing concern for fair apportionment" by rejecting the District's apportionment formula based wholly on the sales factor:

> "The great majority of States imposing corporate income taxes apportion the total income of a corporation by application of a three-factor formula which gives equal weight to the geographical distribution of plant, payroll, and sales. The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to them-

selves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves. Conversely, in some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in the three-factor jurisdictions so that only 33% of their incomes will be subject to state taxation. In any case, the sheer inconsistency of the District formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and an uneconomic pattern of plant location, and so presents an added reason why this Court must give proper meaning to the relevant provisions of the District Code." 380 U.S. 553, 559-560.

That decision in 1964 provided a strong thrust toward uniformity, as evidenced by the wide spread adoption of the Uniform Division of Income for Tax Purposes Act and the fact that of the 46 jurisdictions presently imposing a corporate tax on net income, only Iowa imposes a statutory single-factor sales formula. In contrast, at the time of the *General Motors* decision, the Court noted a broader variety of state tax practices among the 38 states then having a corporate income tax, with 29 using a three-factor formula, three using a two-factor formula involving sales and property and four using formulae based on the geographic distribution of corporate sales. 380 U.S. 553, 559, Footnote 9.

The decision of the Iowa supreme court sustaining the constitutionality of this lone deviation, if left standing, would operate as a powerful centrifugal force in state taxation of interstate commerce, subvert the clear direction provided by this Court in *General Motors*, and provide a basis for new state tax burdens on interstate commerce tending to balkanize the common market of the United States.

The Iowa supreme court completely ignored this Court's express concerns about multiple taxation with the potential of "unhealthy fragmentation of enterprise and an uneconomic pattern of plant location . . . ." 380 U.S. 553, 560, and the clear admonition of possible constitutional problems when the Court stated:

"We of course do not mean to take any position on the constitutionality of a state income tax based on the sales factor alone. *For the present purpose, it is sufficient to note that the factors alluded to by this Court in justifying apportionment measures constitutionally challenged in the past lend little support to the use of an exclusively sales-oriented approach.* (Emphasis added). 380 U.S. 553, 561.

The Iowa supreme court ignored the district court's finding of fact that double taxation was the result of imposition of the Iowa tax. Indeed, double taxation is inherent and inevitable if a state chooses to use a single-factor sales formula when most other jurisdictions use a three-factor formula. The Iowa court stated, erroneously, that because a corporation is entitled to deduct from its taxable income one-half of the federal income tax it pays, impermissible double taxation will not result. 254 NW 2d 737, 751. This ignores the crucial fact, which is that the fraction which Iowa applies to the income figure has as its numerator sales in Iowa and as its denominator total sales, which, as this Court observed in *General Motors* could lead to 100% of a corporation's income being taxed in Iowa, and 67% of its income being taxed in other states which use the standard three-factor formula.

The deduction which the Iowa supreme court holds is a palliative against any double taxation is for 50% of that portion of the federal income tax "as is fairly and equitably allocable to Iowa", Code §422.35. The court does not expound upon how this deduction avoids double taxation. It says, after mentioning the deduction, that "Clearly, a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales." 254 NW 2d 737, 751. But this is true under any taxing statute which provides for deductions, as almost all such statutes do. The pertinent question, however, is, not whether Iowa taxes all the income from Iowa sales, but rather, does Iowa tax any income which is not permissibly attributable to Iowa, resulting in that double taxation which is repugnant to the Constitution.

The invidious impact of the Iowa tax can be seen from two examples. Assume first a corporation whose properties or payroll in Iowa were non-existent or negligible in comparison to those located elsewhere, but which nonetheless sold all its

production in Iowa. Leaving aside some minor adjustments provided by statute, after giving effect to the deduction for 50% of federal taxes paid on income which Iowa allocates to itself, approximately 76% of that income will be taxed in Iowa.* However, states in which that corporation's property and employees are located, which employ the three-factor formula, will tax 67% of its income, including that portion already taxed by Iowa, with the result that 143% of its income will be taxed—not unlike this case, where the district court found, as a fact, that the Iowa formula resulted in 141.76% of Moorman's income being taxed.

Compare this impact upon a foreign corporation selling in Iowa with the impact upon an Iowa corporation selling all its goods in other states. In that case, the corporation would pay no income tax to Iowa with respect to such out-of-Iowa sales, and the other states, which employ a three-factor formula, would tax only 33% of its income, since they would only have the sales factor to apply, the other two factors (property and payroll) being attributable to Iowa.

Thus we have an Iowa corporation selling elsewhere being taxed on only 33% of its income, while a foreign corporation in Iowa is taxed on 143% of its income. This is the sort of tax climate which will lead to what this Court was concerned about in *General Motors*—an unhealthy fragmentation of enterprise and uneconomic pattern of plant location.

The burgeoning growth of state government drives legislators to seek new sources of revenue. In a state such as Iowa, second only to California in agricultural production, the revenues of foreign manufacturing corporations are an attractive target, especially when they are tapped by a tax which gives a competitive market advantage to local industry.

The interstate commerce to Iowa conducted by Association members alone is of major significance. 1976 Association data show 2,157,000 vehicles registered in Iowa. 1,573,000 were automobiles and 584,000 were commercial vehicles, operated by 1,926,000 licensed drivers. In 1976 alone, the Iowa formula burdened interstate commerce by extracting over $3,700,000 in taxes from Association members which would not be payable under the three-factor formula.

*100% minus 24%, being 1/2 of the 48% federal corporate income tax rate.

The result of permitting the Iowa supreme court's decision to stand will be that situation which the framers of the Constitution sought to avoid by the Commerce Clause. This Iowa tax has created a protectionist wall favoring local corporations and giving them a competitive advantage over corporations like the Association's members listed previously, for the latter will be taxed on more than 100% of their income, while the former will be taxed on less than 100% of their income.

Iowa's tax projects its taxing powers beyond its borders, and in so doing denies to the Association's members due process:

> "The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due. A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to 'project the taxing power of the state plainly beyond its borders'." *Norfolk & W. Ry Co.* v *Missouri State Tax Commission*, 390 US 317, 325 (1968).

For the foregoing reasons, the Association urges that this Court take jurisdiction and confirm the equitable guidance it provided in 1964 towards a nationally harmonious state taxation policy.

Respectfully submitted,

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IN THE

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Appellant

v.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Appellee

On Appeal from the Supreme Court of the State of Iowa

MOTION OF THE COMMITTEE ON STATE TAXATION OF THE COUNCIL OF STATE CHAMBERS OF COMMERCE FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND BRIEF OF *AMICUS CURIAE* IN SUPPORT OF APPELLANT'S JURISDICTIONAL STATEMENT

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The Committee on State Taxation of the Council of State Chambers of Commerce ("COST") hereby respectfully moves for leave to file the attached Brief *Amicus Curiae* in Support of Appellant's Jurisdictional Statement. The consent of the attorney for the Appellant has been obtained. The consent of the attorney for the Appellee was requested but refused. The Appellant's letter of consent and the Appellee's letter of refusal are submitted herewith.

COST consists of over 100 companies which have multi-state operations and derive income from multi-state sources. The members of COST have a vital interest in the uniform apportionment of income among the states and in the prevention of multiple state taxation. COST has long been involved in the study of interstate business transactions and both COST and its members have accumulated a great deal of expertise with respect to interstate taxation. Accordingly, COST believes it can make a significant contribution to the Court's consideration of Appellant's Jurisdictional Statement.

Respectfully submitted,

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BRIEF OF THE COMMITTEE ON STATE TAXATION OF THE COUNCIL OF STATE CHAMBERS OF COMMERCE AS *AMICUS CURIAE* IN SUPPORT OF APPELLANT'S JURISDICTIONAL STATEMENT

QUESTION PRESENTED

Whether net income tax on corporations imposed by the Code of Iowa, which attributes to Iowa 100% of the income from the sale of goods manufactured without Iowa, but sold within Iowa, so discriminates against interstate commerce as to violate the Commerce Clause and so unfairly apportions the income derived from such activity as to offend due process.

INTEREST OF THE AMICUS

The interest of the *Amicus* Committee on State Taxation of the Council of State Chambers of Commerce (COST), which consists of over 100 companies deriving income from multi-state sources, is set out in the accompanying motion of COST for leave to file this brief as *amicus curiae*.

ARGUMENT

The Court should hear this case because it presents an important constitutional issue concerning state taxation of interstate commerce—whether a single sales-factor apportionment formula violates the Commerce Clause of the Constitution and the due process clause of the Fourteenth Amendment—which this Court discussed, but did not decide, in *General Motors Corporation* v. *District of Columbia*, 380 U.S. 553. Iowa's single "sales-factor formula" violates the Commerce Clause for two reasons: it leads ineluctably to multiple taxation of foreign corporations doing business in Iowa, and it inevitably discriminates against interstate commerce by affording local manufacturers a competitive advantage over their foreign rivals. In addition, Iowa's tax offends due process by arrogating corporate income to the state out of all proportion to the business activities within the state. The Court also should hear the appeal of Moorman Manufacturing Company because its affirmance of the judgment below would undermine the gains toward uniformity of apportionment formulae which *General Motors* has promoted and would encourage an emerging trend toward parochial and protectionist state taxation of interstate commerce.

1. Iowa imposes an income tax on corporations whose business is carried on partly within and partly without the state. Where a corporation's income is derived from the manufacture or sale of goods both within and without the state, Iowa employs a single "sales-factor formula" under which the corporation's apportionable net income [1] is attributed to Iowa "in that proportion which the gross sales made within the state bear to the total gross sales." Section 422.33(1)(b), Code of Iowa.[2]

In *General Motors* the Court considered a single "sales-factor formula" and found it unauthorized by statute. While not deciding the constitutional question, the Court's statutory analysis found "support in the consequences which a contrary view would have for the over-all pattern of taxation of income derived from interstate commerce." 380 U.S. at 559. The Court added that the fact that "the sheer inconsistency of the District [sales-factor] formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and an uneconomic pattern of plant location" was "an added reason" supporting its statutory construction. 380 U.S. at 560. With Iowa's similar statute now conclusively construed by the state Supreme Court, those "consequences" have been actualized, and the constitutional questions must be faced.

Iowa is the only state requiring the division of income on the basis of the single "sales-factor formula" (J.S. App. A, p. A5; J.S. App. B, p. A37). Forty-four [3] of

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[1] Certain income of the corporation, such as interest, dividends, rents and royalties, is wholly attributed to the state of its geographic source. Section 422.33(1)(a), Code of Iowa. The remainder of the corporation's net income is apportioned.

[2] Sales are attributed to the state of destination, not of origin. Section 422.33(1)(b), Code of Iowa.

[3] Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Utah, Vermont, Virginia and Wisconsin.

the forty-five other states (including the District of Columbia) which impose a corporate income tax utilize a three-factor apportionment formula which takes into account the geographical distribution of a corporation's payroll, property and sales.[4] Thus, this case does not present the Court with the task of choosing between the Iowa and Illinois apportionment formulae. Rather, the question before the Court is whether the Iowa apportionment formula, which is "seriously at variance with those prevailing in the vast majority of States and creates substantial dangers of multiple taxation" (*General Motors, supra*, 380 U.S. at 556-557), violates the Commerce Clause and denies due process.

2. Iowa's deviate single sales-factor formula violates the Commerce Clause because it leads ineluctably to multiple taxation of foreign corporations doing business in Iowa. As this Court noted in *General Motors, supra*, 380 U.S. at 559-560:

> The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves.

Iowa has recognized that its taxing system has precisely this result. Appellee Bair acknowledged in his opinion affirming the assessment against Moorman Manufacturing Co. (Moorman) that "because of the differences in the

[4] Colorado also has a two-factor property and sales formula, and Missouri a one-factor sales formula, which are available to taxpayers at their option as alternatives to the three-factor formula. The forty-fifth state, West Virginia, uses a two-factor formula which omits the sales component of the traditional three-factor formula.

types of apportionment formulae and tax bases among the states, double taxation can and does result" [5] (J.S. App. A, p. A6).

While a state may impose a net income tax on the portion of a foreign corporation's net income earned from, and fairly apportioned to, the taxing state (*Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U.S. 450), it is equally settled that a state may not "impose a tax which discriminates against interstate commerce * * * by subjecting interstate commerce to the burden of 'multiple taxation' * * *." *Id.* at 458; *see also Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 157; *J.D. Adams Manufacturing Co.* v. *Storen*, 304 U.S. 307.

3. The same interaction of Iowa's unique single sales-factor formula with the other states' evenhanded three-

[5] The district court found on stipulated facts that (in 1968) Illinois, applying the three-factor formula, apportioned to itself 41.76% of the income from sales to Iowa customers of goods manufactured in Illinois, because of associated plant and payroll in Illinois. Iowa, using its single sales-factor formula, attributed to itself 100% of the income from the same sales. Thus, "the total percentage of income [from Iowa sales] which must bear a corporate tax between these two states [is] 141.76% (J.S. App. B, p. A36).

The Supreme Court of Iowa's rejection of this finding is unpersuasive. That court denied that double taxation had been shown because it found that "a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales" (J.S. App. C, p. A82). The Court reached this conclusion because of certain "potentially large" deductions from federal "taxable income" allowed in calculating Iowa net income, such as a deduction for 50% of the corporation's federal tax liability. This ignores the fact that certain additions, as well as deductions, are made to federal taxable income in arriving at Iowa net income. Section 422.35, Code of Iowa. In any event, the definition of "net income" is irrelevant to the issue of apportionment. Here, as the district court found, Iowa apportioned to itself 100% of Moorman's net income from sales to Iowa customers. This Court recognized in *General Motors* that a single sales-factor apportionment formula results in the attribution of 100% of the income in question to the jurisdiction having such a formula. *General Motors, supra*, 380 U.S. at 557, 560.

factor approach inevitably discriminates against interstate commerce by affording local manufacturers a competitive advantage over their foreign rivals. The Court noted this consequence in *General Motors*, *supra*, 380 U.S. at 560.

> [I]n some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in the three-factor jurisdictions so that only 33% of their incomes will be subject to state taxation.

The district court observed this precise effect in this case of Iowa's single sales-factor formula (J.S. App. A, p. A38).

> While Moorman's business in Iowa is subjected to the double tax of both Iowa and Illinois, a similarly situated Iowa interstate manufacturer shipping goods, for example, to Illinois would pay taxes only in Illinois; then on the one-third portion of its business activity there represented by its Illinois sales.

Iowa's single sales-factor formula affords this commercial advantage to Iowa-based manufacturers, not only in relation to Illinois-based competitors, but over all interstate businesses making sales in Iowa whose plants and payroll are located in any of the forty-five other states that impose a corporate income tax, because all of the other forty-five states utilize property and payroll in their apportionment formulae.[6] *See supra* pp. 3-4.

The granting of such advantages to local enterprises, which are withheld from foreign corporations, violates

[6] This advantage would exist to a lesser extent over such interstate businesses operating in both Iowa and Colorado which elect to use Colorado's alternative two-factor property and sales apportionment formula. The advantage would not exist over interstate businesses operating in both Iowa and Missouri which elect to use Missouri's alternative single sales-factor apportionment formula. *See supra* p. 4 n. 4.

the Commerce Clause. In *Northwestern States Portland Cement Co.* v. *Minnesota*, *supra*, 358 U.S. at 458, this Court observed that a state may not "impose a tax which discriminates against interstate commerce * * * by providing a direct commercial advantage to local business, *Memphis Steam Laundry* v. *Stone*, 342 U.S. 389 (1952); *Nippert* v. *Richmond*, 327 U.S. 416 (1946) * * *."

4. In addition, Iowa's tax offends due process by arrogating corporate income to the state out of all proportion to the business activities within the state. This Court has held that a state may impose a tax on a foreign corporation doing business within the state, "if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society." *Wisconsin* v. *J.C. Penney Co.*, 311 U.S. 435, 444. That requirement is satisfied "if the tax is fairly apportioned to the commerce carried on within the State." *Ott* v. *Mississippi Valley Barge Line Co.*, 336 U.S. 169, 174; *Northwestern States Portland Cement Co.* v. *Minnesota*, *supra*, 358 U.S. at 452.

For this reason, the Court held in *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission*, 390 U.S. 317, 325, n.5:

> A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to "project the taxing power of the state plainly beyond its borders." *Nashville, C. & St. L.R. Co.* v. *Browning*, 310 U.S. 362, 365 (1940). Any formula used must bear a rational relationship, both on its face and in its application, to property values connected with the taxing state. *Fargo* v. *Hart*, 193 U.S. 490, 499-500 (1904) [footnote omitted].

And in *General Motors, supra,* 380 U.S. at 561, in criticizing the single sales-factor formula, the Court recalled that "it has sought to ensure that the [income apportionment] methods used display a modicum of reasonable relation to corporate activities within the State." Noting that an income apportionment formula should approximate "the distribution of either a corporation's sources of income or the social costs which it generates," the Court concluded that "the geographic distribution of a corporation's sales is, by itself, of dubious significance in indicating the locus of either factor." *Id.*

Iowa's single sales factor fails to satisfy these requirements of due process on the facts of this case. On the basis of stipulated facts the district court found (J.S. App. B, pp. A28-A29):

> Since the largest quantum of capital and labor respecting its [Moorman's] product sold here results from its Illinois relationship, the Iowa apportionment formula fails to reasonably apportion profits traceable to Illinois operations and taxes those activities occurring in Illinois.

In reversing, the Supreme Court of Iowa did not dispute the factual conclusion of the district court, but nevertheless found that the Iowa formula (J.S. App. C, pp. A78-A79)

> is fairly calculated to assign to Iowa only that portion of the taxpayer's net income reasonably attributable to the trade or business done in Iowa since the taxing power exerted by this statute bears fiscal relation to the protection, opportunities and benefits given by the state.

The formulation by the Supreme Court of Iowa confuses the due process requirement of a nexus sufficient to support the exercise of a state's taxing power[7] (never in

[7] See *Wisconsin* v. *J.C. Penney Co., supra.*

dispute here) with the due process requirement that the tax be "fairly apportioned to the commerce carried on within the State." *Ott* v. *Mississippi Valley Barge Line Co., supra,* 336 U.S. at 174. To satisfy the former is not necessarily to meet the latter. Here, the stipulated facts conclusively show that Iowa attributes to itself income "out of all appropriate proportion to the business transacted" in Iowa. *Hans Rees' Sons, Inc.* v. *North Carolina,* 283 U.S. 123, 135. In so doing it denies due process.

5. The Court's affirmance of the judgment below would undermine the gains toward uniformity of apportionment formulae which *General Motors* has promoted and would encourage an emerging trend toward parochial and protectionist state taxation of interstate commerce. This Court's decision in *General Motors, supra,* was an important incentive for the development of uniform taxation of income derived from interstate commerce. However, the court below has seized on the fact that the decision was statutory to ignore its basic teaching and to sustain a unique and aberrant taxing scheme.

The use of a three-factor property, payroll and sales apportionment formula by forty-four of the forty-six states with corporate income taxes represents the culmination of a continuing movement toward use of the three-factor formula during this century. While there still are differences among the states in their definitions of "property," "payroll" and "sales," the use of the same three factors in their apportionment formulae is an important step toward complete uniformity of apportionment formulae and thus toward elimination of multiple taxation.

In 1929, the sixteen states with corporate income taxes used eleven different apportionment formulae, the most popular of which were a one-factor formula based on property and a one-factor formula based on sales. By 1953, fifteen formulae were in use, but sixteen of the thirty-five states with corporate income taxes employed

the three-factor formula. Special Subcommittee on State Taxation of Interstate Commerce, House Committee on the Judiciary, *State Taxation of Interstate Commerce*, H.R. Rep. No. 1480, 88th Cong., 2d Sess. (Vol. 1) 119 (1964). The movement toward uniformity of factors was further aided by the adoption in 1957 by the National Conference of Commissioners on Uniform State Laws of the Uniform Division of Income for Tax Purposes Act (UDITPA), which provides in § 9 for a three-factor apportionment formula based on property, payroll and sales.[8]

In 1963, shortly before this Court's decision in *General Motors*, twenty-six of the thirty-eight states with corporate income taxes used the three-factor formula, and the number of different formulae in use had declined to eleven. *State Taxation of Interstate Commerce, supra*, at 119. As noted above, this Court's disapproval of the single sales-factor formula in *General Motors* in 1965 further accelerated that trend, so that today forty-four of the forty-six states taxing corporate income use the three-factor formula.

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[8] The Multistate Tax Compact was adopted in response to the enactment by Congress of P.L. 86-272, 73 Stat. 555 (1959) [15 U.S.C. §§ 381-84], and the introduction of H.R. 11798, 89th Cong., 1st Sess. (1965), as the result of the Congressional study of state taxation of interstate commerce mandated by P.L. 86-272. The acknowledged purpose of the Compact was to preempt potential Congressional legislation dealing with protection of interstate commerce from discriminatory taxation. The Compact, whose constitutionality is now at issue in this Court in another appeal, copied UDITPA.

The Multistate Tax Commission created by the Compact has been inconsistent in its support of the equally weighted three-factor formula required by UDITPA. For example, Florida, one of the seven founding members, was continued by the Commission as a full member of the Compact notwithstanding that state's adoption of a discriminatory double-weighted sales factor which violated the specific terms of the Compact. Moreover, the Multistate Tax Commission has promulgated regulations which obliterate key elements of UDITPA, particularly with respect to non-business income and the so-called unitary business-combined return concept.

Iowa's single sales-factor apportionment formula is a glaring exception to this trend. However, beginning in 1971, four states which utilize three-factor apportionment formulae—Florida, Wisconsin, New York and Massachusetts—have moved in the direction of Iowa's discrimination against out-of-state businesses by attributing double weight to the sales factor of the apportionment formula, a practice which incorporates to a lesser degree the vice of Iowa's single sales-factor formula.[9] The Court's refusal to hear the Moorman appeal would accelerate this emerging trend away from an equally weighted three-factor formula and thus would jeopardize the gains that have been made toward uniformity of apportionment and reduction in multiple taxation.

CONCLUSION

For the foregoing reasons, jurisdiction of this appeal should be noted.

Respectfully submitted,

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Of Counsel: *Attorneys for Amicus Curiae*

PATTON, BOGGS & BLOW

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[9] In addition, a bill providing for double weighting of the sales factor was introduced in the Illinois State Senate on April 7, 1977. The bill, S.B. 737, came up for a final vote by the Senate on May 26, 1977, but was recommitted to the Senate Revenue Committee for further study of its revenue impact.

MOTION FILED
OCT 21 1977

IN THE

SUPREME COURT

OF THE

UNITED STATES

OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

v.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

MOTION TO FILE AN AMICUS CURIAE BRIEF IN SUPPORT OF APPELLANT

The Multistate Tax Commission hereby requests permission to file the attached Amicus Curiae Brief in support of this Court noting probable jurisdiction in the captioned matter for the reasons stated therein.

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STATE PRINTING PLANT ◆ OLYMPIA, WASHINGTON

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Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

BRIEF FOR THE MULTISTATE TAX COMMISSION AS AMICUS CURIAE IN SUPPORT OF APPELLANT'S POSITION REGARDING JURISDICTION

I.

STATEMENT OF INTEREST

The Multistate Tax Commission (hereinafter referred to as the Commission) is the official administrative agency of the Multistate Tax Compact (hereinafter referred to as the Compact) entered into cur-

rently by 19 states as full members, and by 13 states as associate members.[1]

The purposes of the Compact are to:

1. Facilitate proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax basis and settlement of apportionment disputes.

2. Promote uniformity or compatibility in significant components of tax systems.

3. Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.

4. Avoid duplicate taxation.

In fulfillment of these objectives in the area of State income taxation of multistate businesses, Article IV of the Compact sets forth the provisions of the Uniform Division of Income for Tax Purposes Act promulgated by the National Conference of Commissioners on Uniform State Laws in 1957 for the allocation and apportionment of income. It apportions "business income" in accordance with the well recognized three factor apportionment formula of property, payroll, and sales, commented on by this Court in *General Motors Corporation vs. District of Columbia*, 380 U.S. 553 (1965).

Article VII permits the Commission to promul-

[1]The current regular members are the states of Alaska, Arkansas, California, Colorado, Hawaii, Idaho, Kansas, Michigan, Missouri, Montana, Nebraska, New Mexico, Nevada, North Dakota, Oregon, South Dakota, Texas, Utah and Washington.
The current associate members are the states of Alabama, Arizona, Georgia, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, Ohio, Oklahoma, Pennsylvania, Tennessee, and West Virginia.

gate advisory rules and regulations concerning this Uniform Act. The Compact also provides joint audits at the request of member states who further implement uniform enforcement of the Uniform Act. In this manner, the Compact and the Commission have sought to substantially diminish potential problems of overtaxation or undertaxation of the income of enterprises carrying on business activities in two or more states or countries. The Commission is thus concerned with purpose for, the operative effect of, and the validity of any state income tax apportionment formula that substantially deviates from the generally accepted and well recognized formula contained in Article IV of the Compact.

II.

ARGUMENT IN SUPPORT OF JURISDICTION

Although as indicated in *General Motors Corporation vs. District of Columbia, supra;* 380 U.S. 553 (1965) the sales factor apportionment formula may be constitutionally suspect in apportioning the net income of a manufacturing enterprise, we do not perceive this to be the basic issue in this cause. Rather, we believe the basic issue is whether or not Iowa's sales factor apportionment formula was intended to or in practical operation and effect discriminates against out-of-state manufacturers or interstate commerce in favor of instate manufacturers or intrastate commerce. We thus believe that this Court should note probable jurisdiction in this case

and apply the standards and rationale in such cases as *Boston Stock Exchange, et al vs. State Tax Commission*, 429 U. S. 318 (1977) and cases cited therein including *Halliburton Oil Well Company vs. Reily*, 373 U.S. 64 (1963).

Therefore it is respectfully submitted that this Court take jurisdiction of this cause for resolution of the discrimination issue.

Respectfully submitted,

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Supreme Court, U. S.
FILED
DEC 27 1977
MICHAEL RODAK, JR., CLERK

APPENDIX

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

DOCKETED SEPTEMBER 22, 1977

PROBABLE JURISDICTION NOTED NOVEMBER 14, 1977

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BEFORE THE STATE DEPARTMENT OF REVENUE
Lucas State Office Building
Des Moines, Iowa

IN THE MATTER OF THE CORPORATION INCOME TAX LIABILITY OF MOORMAN MANUFACTURING COMPANY, 1000 NORTH 30th STREET, QUINCY, ILLINOIS 62310

ORDER

This matter came on for hearing before the Director of Revenue on October 24, 1974. Present on behalf of the taxpayer were Walter R. Brown and John V. Donnelly, Attorneys. Present on behalf of the Director of Revenue were Ronald Amosson, Director, Income Tax Division, John Christensen, Auditor, Corporation Audit Section, and Harry M. Griger, Assistant Attorney General.

STATEMENT OF FACTS

The taxpayer, a corporation, is a manufacturer with its principal place of business at Quincy, Illinois. The taxpayer does no manufacturing in Iowa and its products which are delivered within Iowa are manufactured and sold within the State of Illinois. For the taxpayer's fiscal years ending March 31, 1968, March 31, 1969, March 31, 1970, March 31, 1971, and March 31, 1972, an assessment for additional corporation income tax was issued by the Department of Revenue against the taxpayer. The taxpayer protested this assessment and raised, prior to and at the hearing, four questions. Two of these questions

have been resolved between the Department and the taxpayer and are no longer in controversy. One of these questions related to the treatment of related expenses in §422.33(1)(a) of the Iowa Code. Taxpayer's computation of such expenses per its tax returns was accepted by the Department for the years in question. The second question involved the definition of "gross sales of the corporation within the state" in §422.33(1)(b) of the Code prior to amendment in §§37 and 38, Chapter 165, Acts of 64th General Assembly, First Session (1971). Prior to such amendment, the numerator of the statutory Iowa sales factor apportionment formula required that both the sale and delivery of the goods occur in Iowa. The amendment to this statute requires that only the delivery of the goods occur in Iowa in order that such sales be contained in the numerator of the formula. For the fiscal years ending March 31, 1968 through March 31, 1971, a portion of the taxpayer's sales which were included by the Department in the numerator of the single sales factor formula were made in Illinois with delivery in Iowa. Consequently, the assessment must be adjusted because such sales should have only been contained in the demoninator of the formula.

Therefore, the taxpayer presents two issues which the Director of Revenue must resolve. These are: (1). Whether the Department of Revenue may make additional income tax assessments within the six months limitation period set forth in §422.25(1) of the Iowa Code where such tax assessment is unrelated to any adjustment in the taxpayer's federal taxable income, and (2). Whether the Iowa single sales factor apportionment formula operated to subject the taxpayer to taxation on a greater portion of its net income than is reasonably attributable to taxpayer's business or sources within Iowa.

CONCLUSIONS OF LAW

The first issue involving the Department's authority to make an assessment of additional Iowa tax unrelated to adjustments in federal taxable income involves only the years ending March 31, 1968 and March 31, 1969. The formal tax assessment was issued on December 22, 1972. This assessment was issued within six months from the date of final disposition of controversy between the taxpayer and the Internal Revenue Service with respect to the years in question. However, the taxpayer contends that during this six months period, the Department was not authorized to assess Iowa tax on the ground of rejection of taxpayer's returns filed on a three factor formula basis and requirement of computation of Iowa income on the basis of the Iowa statutory single sales factor formula. The first sentence in §422.25(1) of the Iowa Code provides in relevant part:

> "1. As soon as practicable and in any event within three years after the return is filed the department shall examine it and determine the correct amount of tax, and the amount so determined by the department shall be the tax; . . ."

For the two fiscal years in question, this three year limitation period had expired prior to the issuance of the Department's assessment of December 22, 1972. During this period and in 1972, §422.25(1) provided in the second sentence thereof:

> *"Notwithstanding the periods of limitation for examination and determination heretofore specified,* the department shall have six months from the date of final disposition of any controversy between the taxpayer and the internal revenue service with respect to the particular tax year to make *the* examination and determination. (emphasis supplied).

The taxpayer contends that this above quoted second sentence of §422.25(1) of the Code only authorized the Department to make adjustments during the six months period which result from a change in federal taxable income and do not authorize the Department to make an adjustment and concomitant assessment due to a change from the three factor to single factor formula unrelated to any "controversy" with the Internal Revenue Service. However, taxpayer's contention ignores the plain meaning of this second sentence of §422.25(1) which clearly gives the Department additional time to make whatever adjustments, whether related to federal taxable income or not, necessary for a proper determination of taxpayer's Iowa income tax liability. To adopt taxpayer's contention is to read into this unambiguous statute words which are not there. Consequently, the Director concludes that the Department properly could, during the six months period, determine that the taxpayer improperly apportioned income to Iowa on the basis of a three factor formula and, thereby, assess taxpayer additional tax and interest on the basis of the Iowa single sales factor formula. The assessment of December 22, 1972, was timely made.

The second issue for the Director of Revenue to resolve on taxpayer's appeal is whether the taxpayer is entitled to file its income tax returns for all the fiscal years in question on the basis of an apportionment formula giving equal weight to sales, property and payroll or whether the Department can properly require the taxpayer to so file on the basis of the statutory single sales factor formula.

The taxpayer contends that a single sales factor formula inherently violates the commerce and due process clauses of the United States Constitution as applied to the states and, in the alternative, contends that it would be

an abuse of discretion by the Director of his authority contained in §422.33(2) of the Iowa Code to refuse the request of taxpayer, which does no manufacturing in Iowa, for permission to use a three factor formula.

A three factor formula consisting of property, payroll, and sales has been expressly held to be valid and constitutional by the United States Supreme Court. *Butler Brothers* v. *McColgan*, 1942, 315 U.S. 501, 62 S.Ct. 701, 86 L.Ed. 991; *General Motors Corporation* v. *District of Columbia*, 1965, 380 U.S. 553, 85 S.Ct. 1156, 14 L.Ed.2d 68. Iowa is the only state requiring apportionment of income on the basis of a single factor formula. Most states allow corporations to file state income or franchise tax returns on the basis of some form of three factor formula, consisting of property, payroll and sales. The formulae in effect in the states differ as to the tax bases to which such formulae apply. In the instant situation, the taxpayer would owe Iowa less tax on the basis of a three factor formula than on a single factor sales formula. Taxpayer, in support of its argument for use of a three factor formula, relies almost totally on *General Motors Corporation* v. *District of Columbia*, supra. While the Supreme Court criticized the use of a single factor sales formula, such criticism was within the context of a statute which did not authorize the use of such a formula, but seemed to require the use of a three factor formula. On the other hand, the following cases support the constitutionality of single factor apportionment formulae: *National Leather Co.* v. *Massachusetts*, 1928, 277 U.S. 413, 48 S.Ct. 534, 72 L.Ed. 935 (Single Property factor); *Underwood Typewriter Co.* v. *Chamberlain*, 1920, 254 U.S. 113, 41 S.Ct. 45, 65 L.Ed. 165 (Single Property factor); *Bass, Ratcliff & Gretton Ltd.* v. *State Tax Commission*, 1924, 266 U.S. 271, 45 S.Ct. 82, 69 L.Ed. 282 (Single assets factor); *Kent-Coffey Mfg. Co.* v. *Maxwell*, 1933, 204 N.C. 365, 168 S.E. 397,

90 A.L.R. 476, aff'd 291 U.S. 642, 78 L.Ed. 1040 (Single property factor); *Ford Motor Co.* v. *Beauchamp*, 1939, 308 U.S. 331, 60 S.Ct. 272, 84 L.Ed. 304 (Single gross receipts factor).

Moreover, because of the differences in the types of apportionment formulae and tax bases among the states, double taxation can and does result. And the use of formulae by other states where the taxpayer does business is not relevant. In *Commonwealth* v. *South Philadelphia Terminal, Inc.*, 1961, 404 Pa. 293, 171 A.2d 758, the Court stated at 171 A.2d 759:

> "The conclusion that the fairness of an allocation formula cannot be determined by consideration of or the effect of a different formula used by another state is most proper. The sole issue is whether Pennsylvania's formula justly allocates to itself a proper portion of the corporation's activities, regardless of the methods used by the other states."

This is also the issue under §422.33(2) of the Iowa Code. For all that appears, apportionment of the taxpayer's income by means of geographical distribution of sales of a unitary business is just as reasonable as the use of other formulae—a position taken by the State Board of Tax Review in *Phillips Petroleum Company* v. *Briggs*, Case No. 47, June 20, 1973. Apportionment formulae are simply approximations of the distribution of the sources of income of a unitary business or the social costs which such business generates. An iron rule of equality of taxation is neither possible nor attainable in this area. Merely because, under some circumstances, the use of a three-factor formula apportions less income to Iowa than the use of a single factor formula is not the test. While it is true that Iowa's single factor formula does not give effect to the

corporation's geographical distribution of property and payroll, there is no constitutional or statutory requirement that it must. "The Constitution is not a formulary". *Wisconsin* v. *J. C. Penney Co.*, 1940, 311 U.S. 435, 444, 61 S.Ct. 246, 85 L.Ed. 267.

The Director of Revenue finds that the Iowa single sales factor formula does not operate to subject taxpayer to taxation on a greater portion of his net income than is reasonably attributable to business or sources within this state. No showing has been made by the taxpayer that he is entitled to the use of a three factor formula over the single sales formula for the years in question. Taxpayer's request for permission to us a three factor formula to apportion income to Iowa is denied.

ORDER

It is hereby Ordered that the Income tax assessment be adjusted and revised for the years in question to be $236,890.00 tax plus interest as provided by law.

Done at Des Moines, Iowa, this 17th day of December, 1974.

/s/ G. D. Bair
G. D. Bair, Director, Iowa Department of Revenue

IN THE DISTRICT COURT OF THE STATE OF IOWA
IN AND FOR POLK COUNTY

Equity No. CE 3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

PETITION IN EQUITY

(Filed February 10, 1975)

COMES NOW, the Plaintiff and states:

DIVISION I

1. The Plaintiff, Moorman Manufacturing Company, is a corporation organized and existing under the laws of the State of Illinois, with its home office located in Quincy, Illinois, and doing business in the State of Iowa.

2. The Defendant, G. D. Bair, is the duly appointed Director of Revenue for the State of Iowa, and is the Executive Officer of the Iowa Department of Revenue, a duly authorized and created department of the State of Iowa.

3. That Plaintiff's principal source of income is derived from the manufacture and sale of tangible personal property in many states of the United States.

4. That Plaintiff engages in no manufacturing within the State of Iowa but sells some of its products (tangible personal property) manufactured outside the State of Iowa within the State of Iowa.

5. That Plaintiff reports its income for income tax purposes on a fiscal year ending March 31.

6. That under date of December 22, 1972, D. G. Briggs, Defendant's predecessor in office, issued an Income Tax Assessment Notice against Plaintiff, together with attachments thereto, copies of which are attached hereto as Exhibit A and by this reference incorporated herein as fully as if set forth, relating to Plaintiff's corporate income tax returns for its fiscal years ended March 31, 1968, 1969, 1970, 1971, and 1972.

7. That Plaintiff duly appealed the aforesaid assessment to the Defendant in a timely manner.

8. That a hearing was held before the Defendant concerning said assessment on October 24, 1974.

9. That under date of December 17, 1974, Defendant issued his Order, a copy of which is marked Exhibit B, attached hereto and by this reference incorporated herein as fully as if set forth.

10. That the Plaintiff has timely filed Notice of Appeal from the aforesaid Order of the Defendant, pursuant to the provisions of Chapter 422, Code of Iowa as amended.

11. That Plaintiff's Iowa corporate income tax returns for its fiscal years ended March 31, 1968, March 31, 1969, March 31, 1970, March 31, 1971, and March 31, 1972, were all timely filed as required by statute and disclosed on their face in a clear and unmistakable manner the method used by Plaintiff to allocate and apportion its income to the State of Iowa.

12. • • •

DIVISION II

• • •

DIVISION III

1. That paragraphs 1, 2, 3, 4, 5, 6, 7, 8, 9, 10, and 11 of Division I of this petition are incorporated by reference in this Division III of Plaintiff's petition as fully as if set forth herein.

2. That on its Iowa corporate income tax returns for its fiscal years ended March 31, 1968, 1969, 1970, 1971, and 1972, Plaintiff, after allocating its interest, dividends, rents, and royalties (less related expenses) within and without the State of Iowa, allocated and apportioned the remainder of its net income to the State of Iowa on the ratio that its payroll, property and sales within the State of Iowa bore to its payroll, property and sales, respectively, everywhere in the United States, giving equal weight to the payroll, property and sales factors.

3. That the Defendant, in assessing additional corporation income tax against Plaintiff, as disclosed by Defendant's Order, applied the so-called "statutory single sales factor formula."

4. That the so-called "statutory single sales factor formula" upon which Defendant's Order is based operates to subject Plaintiff to taxation on a greater portion of its net income than is reasonably attributable to its business or sources within the State of Iowa.

5. That the method of allocating and apportioning net income derived by a corporation from the manufacture of tangible personal property outside the State of Iowa which is sold within the State of Iowa as prescribed in paragraph 1 of Section 422.33 of the Code of Iowa (the so-called "statutory single sales factor formula") is unconstitutional in that it:

(a) Violates the due process clause of Section 1 of the Fourteenth Amendment to the Constitution of the United States in that it taxes in its entirety income at least partially attributable to the use of income-producing factors (i.e., labor and capital) outside the State of Iowa.

(b) * * *

(c) Violates Article I, Section 8, Clause 3 of the Constitution of the United States (the commerce clause) in that it subjects to Iowa income tax income from the sale of tangible personal property in Iowa, a portion of which is properly subject to tax in other states.

(d) Violates Article I, Section 8, Clause 3 of the Constitution of the United States (the commerce clause) in that it interferes with and places a burden upon interstate commerce.

(e) Violates the equal protection clause of Section 1 of the Fourteenth Amendment to the Constitution of the United States in that for the purpose of income taxation it subjects income arising from the manufacture of tangible personal property outside the State of Iowa which is sold within the State of Iowa to taxation in the same manner as income arising from both the manufacture and sale of tangible personal property in the State of Iowa and fails to subject income arising from the manufacture of tangible personal property within the State of Iowa which is sold outside the State of Iowa to Iowa income taxation.

(f) * * *

6. * * *

DIVISION IV

1. That paragraphs 1, 2, 3, 4, 5, 6, 7, 8, 9, 10, and 11 of Division I of this petition and that paragraph 2 of Division III of this petition are incorporated by reference in this Division IV of Plaintiff's petition as fully as if set forth herein.

2. That the full and complete disclosure of Plaintiff's method of allocating and apportioning its net income on its Iowa corporate income tax returns constituted a filing by the Plaintiff with the Defendant of its statement of objections to the use of the single sales factor formula in computing Plaintiff's income allocable to the State of Iowa and provided an alternative method of allocation and apportionment as required in paragraph 2 of Section 422.33, Code of Iowa.

3. That Plaintiff's method of allocating and apportioning its net income in its Iowa corporate income tax returns for its fiscal years ended March 31, 1968, 1969, 1970, 1971, and 1972 subjects to Iowa income tax that portion of its net income reasonably attributable to its trade or business within the State of Iowa.

4. That paragraphs 3 and 4 of Division III of this petition are incorporated by reference in this Division IV of Plaintiff's petition as fully as if set forth herein.

5. That the Iowa Department of Revenue and at least some of its Directors (and its predecessor, the Iowa State Tax Commission) have from time to time permitted some foreign corporations to allocate and apportion their net income derived from the manufacture of tangible personal property outside the State of Iowa which is sold within the State of Iowa by methods other than that prescribed by paragraph 1 of Section 422.33 of the Code of Iowa,

including the method used by Plaintiff on its income tax returns for the years at issue here.

6. That Defendant's Order, by failing to permit Plaintiff to allocate and apportion its net income during the years at issue pursuant to a method other than that prescribed by paragraph 1 of Section 422.33 of the Code of Iowa:

(a) Denies Plaintiff the equal protection of the laws in violation of the last clause of Section 1 of the Fourteenth Amendment to the Constitution of the United States in that it subjects Plaintiff's net income for the years at issue to taxation in a manner different from the manner that has been applied to those similarly situated, and for the further reason that it taxes Plaintiff's net income in the same manner as the income of corporations arising from both the manufacture and sale of tangible personal property in the State of Iowa and fails to subject to Iowa taxation the income of corporations arising from the manufacture of tangible personal property within the State of Iowa which is sold outside the State of Iowa.

(b) * * *

(c) * * *

(d) * * *

(e) Deprives Plaintiff of its property without due process of law in violation of Section 1 of the Fourteenth Amendment to the Constitution of the United States in that it taxes in its entirety income at least partially attributable to the use of income-producing factors (i.e., labor and capital) outside the State of Iowa.

(f) * * *

(g) Violates Article I, Section 8, Clause 3 of the Constitution of the United States (the commerce clause) in that it subjects to Iowa income tax Plaintiff's income from the sale of tangible personal property in Iowa, a portion of which is properly subject to tax in other states.

(h) Violates Article I, Section 8, Clause 3, of the Constitution of the United States (the commerce clause) in that it interferes with and places a burden upon interstate commerce.

(i) * * *

(j) * * *

WHEREFORE, Plaintiff prays that the Court overrule and set aside Defendant's Order assessing additional corporation income tax due from the Plaintiff, and for such other relief as the Court deems just and equitable in the premises, and that the cost of this action be taxed to the Defendant.

Swift, Brown and Winick

By /s/ Walter R. Brown
Walter R. Brown

By /s/ John V. Donnelly
John V. Donnelly

1200 Register and Tribune Building
Des Moines, Iowa 50309
(515) 283-2076

Attorneys for Plaintiff

IN THE DISTRICT COURT OF THE STATE OF IOWA
IN AND FOR POLK COUNTY

Equity No. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE
STATE OF IOWA,
Defendant

ANSWER

(Filed February 27, 1975)

COMES NOW, G. D. Bair, Director of Revenue, State of Iowa, defendant, and for Answer to the Petition In Equity filed herein by Plaintiff, respectfully states to the Court as follows:

DIVISION I

1. Paragraph one (1), Division I, of plaintiff's petition is admitted.

2. Paragraph two (2), Division I, of plaintiff's petition is admitted.

3. Paragraph three (3), Division I, of plaintiff's petition is admitted.

4. Paragraph four (4), Division I, of plaintiff's petition is admitted.

5. Paragraph five (5), Division I, of plaintiff's petition is admitted.

6. Paragraph six (6), Division I, of plaintiff's petition is admitted.

7. Paragraph seven (7), Division I of plaintiff's petition is admitted.

8. Paragraph eight (8), Division I, of plaintiff's petition is admitted.

9. Paragraph nine (9), Division I, of plaintiff's petition is admitted.

10. Paragraph ten (10), Division I, of plaintiff's petition is admitted.

11. Paragraph eleven (11), Division I, of plaintiff's petition is admitted.

12. • • •

DIVISION II

• • •

1. For answer to paragraph one (1), Division III, of plaintiff's petition, this defendant realleges his answers in paragraphs one (1) through eleven (11), inclusive, of Division I of this answer, and incorporates them herein in Division III of this answer, the same as if set forth in full.

2. For answer to paragraph two (2), Division III, of plaintiff's petition, this defendant admits that plaintiff, for its fiscal tax years in question, apportioned income derived from manufacture and sale of tangible personal property to Iowa, on its Iowa income tax returns, utilizing a three factor formula consisting of a property factor, a payroll factor, and a sales factor, all equally weighed, but this defendant denies plaintiff was entitled to use the particular formula, as computed by it, or any other three factor formula.

3. Paragraph three (3), Division III, of plaintiff's petition is admitted.

4. Paragraph four (4), Division III, of plaintiff's petition is denied.

5. Paragraph five (5), and each subparagraph thereunder, Division III, of plaintiff's petition are denied.

6. * * *

DIVISION IV

1. For answer to paragraph one (1), Division Iv, of plaintiff's petition, this defendant realleges his answers in paragraphs one (1) through eleven (11), inclusive, in Division I of this answer and realleges his answer in paragraph two (2) of Division III of this answer, and incorporates them herein in Division IV of this answer, the same as if set forth in full.

2. Paragraph two (2), Division IV, of plaintiff's petition is denied.

3. Paragraph three (3), Division Iv, of plaintiff's petition is denied.

4. For answer to paragraph four (4), Division IV, of plaintiff's petition, this defendant realleges his answers in paragraphs three (3) and four (4) of Division III of this answer, and incorporates them herein, the same as if set forth in full.

5. Paragraph five (5), Division IV, of plaintiff's petition is denied.

6. Paragraph six (6) and each subparagraph thereunder, Division IV, of plaintiff's petition are denied.

WHEREFORE, defendant prays that the Court confirm his Order, dated December 17, 1974, which sustained Iowa income taxes assessed against the Plaintiff in the amount of $236,890 tax plus interest as provided by law; for the costs of this action; and for such other relief as the Court deems just and equitable in the premises.

/s/ Donald H. Capotosto
Donald H. Capotosto
Assistant Attorney General

/s/ Harry M. Griger
Harry M. Griger
Assistant Attorney General
Lucas State Office Building
Des Moines, Iowa 50319
Attorneys for Defendant

(Proof of Service Omitted in Printing)

IN THE DISTRICT COURT OF THE STATE OF IOWA
IN AND FOR POLK COUNTY

Equity No. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

STIPULATION

(Filed February 20, 1976)

COME NOW the Plaintiff and the Defendant, by their respective attorneys and stipulate and agree for purposes of this action only that the following facts may be accepted as true and correct, that the documents attached hereto are true and genuine copies of the respective original documents, and that this stipulation may be offered into evidence by either party subject, however, to the right of either party to offer evidence not inconsistent with the facts herein stipulated and subject to the right of either party to object to the relevance and materiality of the facts herein stipulated:

1. The Plaintiff, Moorman Manufacturing Company, is a corporation organized and existing under the laws of the State of Illinois, with its home office located in Quincy, Illinois, and doing business in the State of Iowa.

2. The Defendant, G. D. Bair, is the duly appointed Director of Revenue for the State of Iowa and is the Executive Officer of the Iowa Department of Revenue, a duly authorized and created department of the State of Iowa.

3. That Plaintiff reports its income for income tax purposes on a fiscal year ending March 31.

4. That Plaintiff's Iowa corporate income tax returns for its fiscal years ended March 31, 1968, March 31, 1969, March 31, 1970, March 31, 1971, and March 31, 1972, were all timely filed as required by statute and disclosed on their face the method used by Plaintiff to allocate and apportion its income to the State of Iowa. Copies of these returns are attached hereto as Exhibits 1, 2, 3, 4, and 5, respectively. These returns did not apportion income to Iowa from the sale of tangible personal property pursuant to the single sales factor formula provided for in §422.33(1), Code of Iowa.

5. That under date of December 22, 1972, D. G. Briggs, Defendant's predecessor in office, issued an Income Tax Assessment Notice against Plaintiff, together with attachments thereto, copies of which are attached hereto as Exhibit 6 and by this reference incorporated herein as fully as if set forth, relating to Plaintiff's corporate income tax returns for its fiscal years ended March 31, 1968, 1969, 1970, 1971, and 1972.

6. That Plaintiff duly appealed the aforesaid assessment to the Defendant in a timely manner.

7. That a hearing was held before the Defendant concerning said assessment on October 24, 1974.

8. That under date of December 17, 1974, Defendant issued his Order, a copy of which is marked Exhibit 7, attached hereto and by this reference incorporated herein as fully as if set forth.

9. Attached hereto as Exhibit 8 is a series of schedules consisting of 21 pages prepared by employees of Defendant. All data and figures contained on such schedules were

supplied by Plaintiff to Defendant at Defendant's request or are contained on Plaintiff's Iowa income tax returns for the years in question.

10. That Plaintiff timely filed Notice of Appeal from the aforesaid Order of Defendant to the District Court of the State of Iowa in and for Polk County, pursuant to the provisions of Chapter 422, Code of Iowa, as amended, and this Court has jurisdiction over the parties and the subject matters of this action.

11. • • •

12. • • •

13. Plaintiff filed its first income tax return with the State of Iowa for its fiscal year ended March 31, 1949. Pursuant to approval of the Iowa State Tax Commission, Plaintiff, after allocating its interest, dividends, rents and royalties (less related expenses) within and without the State of Iowa, apportioned the remainder of its net income to the State of Iowa on the ratio that its payroll, property and sales, as computed by Plaintiff, within the State of Iowa bore to its payroll, property and sales everywhere in the United States, as computed by Plaintiff, giving equal weight (1/3 each) to its computed payroll, property and sales factors. This method was used by Plaintiff in each successive income tax return filed with the State of Iowa up to and including the income tax return filed for its fiscal year ended March 31, 1960.

14. For its fiscal years ended March 31, 1961, 1962, 1963, and 1964, Plaintiff determined its income from the sale of tangible personal property in this State pursuant to the single sales factor formula provided for in §422.33 (1) of the Iowa Code at the direction of the Iowa State Tax Commission.

15. Plaintiff resumed computing its income from the sale of tangible personal property attributable to Iowa by application of the aforesaid three-factor formula for its fiscal year ended March 31, 1965, and has applied such formula in each succeeding return filed to date, including those here at issue. While Defendant concedes that Plaintiff did, for the years here at issue, apportion income to Iowa by using a three-factor formula consisting of sales, property and payroll factors, Defendant does not concede that the aforesaid three factors computed and utilized by Plaintiff are uniformly computed pursuant to the laws of the states in which Plaintiff does business or which allow the use of an apportionment formula consisting of sales, property and payroll factors.

16. That the Defendant, in assessing additional corporation income tax against Plaintiff, as disclosed by Defendant's Order, applied the single sales factor formula provided for in §422.33(1) of the Iowa Code.

17. Plaintiff owns all of the outstanding capital stock of Quincy Soybean Co., Quincy, Illinois; Moorman Manufacturing Company of California, Inc., San Gabriel, California; and Bell Grain and Milling, Inc., Perris, California. Bell Grain and Milling, Inc., owns all of the outstanding stock of Bell Milling Corporation, Escondido, California.

18. Plaintiff's principal source of income during the years at issue was and is now the manufacture and sale of more than 80 different products for feeding livestock and poultry, with the greatest portion of its sales derived from mineral and protein supplements for livestock.

19. At all times here relevant Plaintiff had five manufacturing plants, located in Quincy, Illinois; Alpha, Illinois; Comanche, Texas; Hereford, Texas; and Columbus, Nebraska; and neither Plaintiff nor any of its affiliates en-

gaged in any manufacturing whatsoever in the State of Iowa.

20. Except for sales in six states in the southeastern part of the United States, Moorman products are sold directly to farmers and ranchers by a sales force of more than 2,500 salesmen, all of whom are employees paid on a commission basis, in more than 30 states. The products are delivered by contract truckers, except in western states, directly to the farm. Western shipments are in carload quantities only and are delivered by the salesmen.

21. During the years at issue delivery to Iowa customers was typically made from one of six warehouses located in Iowa, at Stanwood, Plainfield, Goldfield, Marcus, Atlantic, and Knoxville.

22. During the years at issue, all of the products sold by Plaintiff in Iowa were manufactured by Plaintiff in the State of Illinois, and none of its affiliates did any business in Iowa.

23. During the years at issue, Plaintiff conducted regular and continuous solicitation in Iowa and made sales from its Iowa warehouses listed in paragraph 21 hereof.

24. During the years at issue, Plaintiff employed approximately the following number of persons in Iowa and in other states:

Date	Iowa Employees	Employees in Other States
3-15-68	518	3,105
3-15-69	553	3,264
3-15-70	562	3,296
3-15-71	582	3,731
3-15-72	562	3,715

The Iowa employees were salesmen and warehouse employees.

25. During the years at issue, Plaintiff paid income taxes to a number of states in addition to Iowa. Attached hereto as Exhibits 9, 10, 11, 12, and 13 are schedules for Plaintiff's fiscal years ended March 31, 1968, 1969, 1970, 1971, and 1972, respectively, which set forth for each state to which Plaintiff paid income taxes the following information for each year, computed as Plaintiff understands the laws of the respective states to require, and which were the basis upon which Plaintiff filed its income tax returns with the various states:

(a) State involved.

(b) Plaintiff's taxable income per its U.S. income tax return.

(c) Plaintiff's net non-business income in each state.

(d) Plaintiff's net business income subject to each particular state's formula method of apportionment.

(e) The percentage of Plaintiff's total property, payroll and sales attributable to each state and the result of dividing the total of these three percentages by three.

(f) Plaintiff's taxable income in each state (the result of multiplying (d) by (e)).

(g) Income tax paid by Plaintiff to each state.

26. Attached hereto as Exhibit 14 is a schedule setting forth for each of the years at issue:

(a) Plaintiff's total sales.

(b) Plaintiff's sales in Iowa.

(c) Plaintiff's sales in Illinois, computed as Plaintiff understands Illinois law to require for Illinois income tax purposes.

(All figures rounded to the nearest dollar.)

27. Attached hereto as Exhibit 15 is a schedule setting forth for each of the years at issue:

(a) Plaintiff's total payroll as computed by Plaintiff for use in the three-factor formula advocated by it for Iowa income tax purposes.

(b) Plaintiff's payroll in Iowa as computed by Plaintiff for use in the three-factor formula advocated by it for Iowa income tax purposes.

(c) Plaintiff's payroll in Illinois, computed as Plaintiff understands Illinois law to require for Illinois income tax purposes.

(All figures rounded to the nearest dollar.)

28. Attached hereto as Exhibit 16 is a schedule setting forth for each of the years at issue:

(a) Plaintiff's total property as computed by Plaintiff for use in the three-factor formula advocated by it for Iowa income tax purposes.

(b) Plaintiff's property in Iowa as computed by Plaintiff for use in the three-factor formula advocated by it for Iowa income tax purposes.

(c) Plaintiff's property in Illinois, computed as Plaintiff understands Illinois law to require for Illinois income tax purposes.

(All figures rounded to the nearest dollar.)

29. Prior to 1961, corporations based outside the State of Iowa were generally permitted by the Iowa State Tax Commission to apportion their net income for Iowa income tax purposes by virtually whatever method they chose, including but not limited to the method used by Plaintiff in the years at issue here.

30. Attached hereto as Exhibit 17 is an analysis prepared by personnel of the Iowa Department of Revenue of apportionment formulae contained in the Iowa corporate income tax returns of non-Iowa manufacturers for the years 1964 through 1972.

Exhibit 17 consists of eight (8) columns setting forth the following information:

Column 1—Year involved.

Column 2—Total number of corporate income tax returns filed by non-Iowa manufacturers.

Column 3—The number of returns (included in Column 2) in which the single (sales) factor method of income apportionment was not used.

Column 4—The number of returns (included in Column 3) using a three-factor formula method of income apportionment consisting of sales, property, and payroll factors, as computed by the corporate taxpayers, which were accepted as filed by Defendant's predecessors or the Iowa State Tax Commission.

Column 5—The number of returns (included in Column 3) in which the use of a three-factor formula method of income apportionment by the taxpayer was denied by Defendant's predecessors or by the Iowa State Tax Commission.

Column 6—The number of returns (included in Column 3) in which the use of a *weighted* three-factor formula (i.e., one-half weighted to sales, one-fourth weighted to property and one-fourth weighted to payroll) method of income apportionment by the taxpayer was denied by Defendant's predecessors or by the Iowa State Tax Commission.

Column 7—The number of returns (included in Column 3) in which the use of a three-factor formula was permitted by the passage of time provided for by the statute of limitations contained in §422.25 of the Iowa Code.

Column 8—The number of returns (included in Column 3) in which the use of a *weighted* three-factor formula was permitted by the passage of time provided for by the statute of limitations contained in §422.25 of the Iowa Code.

31. The parties stipulate and agree that the Court may take judicial notice of the statutes and rulings and regulations of the various departments of the several states and territories of the United States and the District of Columbia (including the Orders of the Iowa State Board of Tax Review) without the necessity of pleading and proof by the parties.

32. * * *

33. The question of law presented for determination in this case are as follows:

I. * * *

II. Constitutionality of the Single Sales Factor Formula.

A. Whether section 422.33(1)(b), Code of Iowa, which requires that net income from the manufacture or sale of tangible personal property be apportioned to the State of Iowa for income tax purposes pursuant to the single sales factor formula is in violation of any of the following provisions of the Constitution of the United States:

1. The due process clause of Section 1 of the Fourteenth Amendment.

2. Article I, Section 8, Clause 3 (the commerce clause).

3. The equal protection clause of Section 1 of the Fourteenth Amendment.

B. * * *

C. * * *

D. * * *

III. Constitutionality of Application of the Single Sales Factor Formula.

If the answers to the questions raised in the immediately preceding subparagraph II are that section 422.33, Code of Iowa, is constitutional, the further questions of law are as follows:

A. Whether Defendant's Order that Plaintiff apportion its net income to the State of Iowa pursuant to the single sales factor formula provided for in section 422.33(1)(b), Code of Iowa, in its application to Plaintiff unconstitutionally:

1. Subjects Plaintiff's net income for the years at issue to taxation in a manner different from the manner that has been applied to those similarly situated, and taxes Plaintiff's net income in the same manner as the income of corporations arising from both the manufacture and sale of tangible personal property in the State of Iowa and fails to subject to Iowa taxation the income of corporations arising from the manufacture of tangible personal property within the State of Iowa which is delivered for transportation outside the State of Iowa, and thereby denies Plaintiff the equal protection of the laws in violation of the last clause of Section 1 of the Fourteenth Amendment to the Constitution of the United States.

2. • • •

3. • • •

4. • • •

5. Taxes in its entirety income at least partially attributable to the use of income-producing factors (i.e., labor and capital) outside the State of Iowa so as to deprive Plaintiff of its property without due process of law in violation of Section I of the Fourteenth Amendment to the Constitution of the United States.

6. • • •

7. Violates Article I, Section 8, Clause 3 of the Constitution of the United States (the commerce clause) in that it subjects to Iowa income tax Plaintiff's income from the sale of tangible personal property in Iowa, a portion of which is properly subject to tax in other states.

8. Interferes with and places an undue burden upon interstate commerce in violation of Article I, Section 8, Clause 3, of the Constitution of the United States.

IV. • • •

34. For the purposes of this action only and without admitting the applicability of any particular formula of apportionment in any other situation, in the event the court finds that the single sales factor formula method of apportionment should not be applied to Plaintiff, Plaintiff's net income from the manufacture and sale of tangible personal property shall be multiplied by the following percentages to determine the portion of that net income apportionable to the state of Iowa:

Plaintiff's Fiscal Year Ended	Apportionment Percentage
3-31-68	14.51%
3-31-69	14.59%
3-31-70	13.88%
3-31-71	13.05%
3-31-72	12.20%

35. The parties respectfully request that following submission of this case, the Court make findings of fact and conclusions of law, but not thereupon enter an appealable Judgment or Order. The parties will attempt

to reach an agreement as to the amount of the deficiency, if any, together with interest as provided by law, owed by Plaintiff to Defendant, within ninety (90) days after the Court has entered its Findings of Fact and Conclusions of Law and submit such agreed-upon amount to the Court as the basis for entry of an appealable Judgment or Order. In the event the parties fail to agree upon the amount of the deficiency, if any, the parties will submit the matter to this Court for its determination, upon the basis of a supplemental stipulation of facts or the submission by the parties of such additional evidence as may be required. It is further requested that no appealable Judgment or Order be issued by the Court until the amount of the deficiency, if any, together with interest as provided by law, has been determined as herein set forth.

Respectfully submitted,

/s/ Harry M. Griger
Harry M. Griger
Counsel for Defendant

/s/ Walter R. Brown
Walter R. Brown

/s/ John V. Donnelly
John V. Donnelly
1200 Register and Tribune Building
Des Moines, Iowa 50309
(515) 283-2076
Counsel for Plaintiff

Date: February 20, 1976

Attached to the Stipulation were certain numbered Exhibits, including the following:

EXHIBIT 8

(EXHIBIT 8 with pages denoted and numbered as exhibits)

EXHIBIT 1-A

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Computation of Tax - Single Factor Formula

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
1. Federal taxable income	10,393,161	11,682,724	13,949,834	13,528,542	13,394,682
2. Add: Iowa income tax	30,294	81,466	106,813	80,528	129,054
3. Interest on state & municipal securities	21,244	28,542	28,390	28,305	4,207
4.	10,444,699	11,792,732	14,085,037	13,637,375	13,527,943
5. Deduct: Federal income tax deduction	2,404,038	3,051,198	3,623,167	3,155,681	3,173,391
6. Interest federal securities	607,632	673,704	986,187	519,496	144,617
7.	3,011,670	3,724,902	4,609,354	3,675,177	3,318,008
8. Net income after adjustments	7,433,029	8,067,830	9,475,683	9,962,198	10,209,935
9. Deduct: Assignable income (exh. #1-B)	356,519	372,369	468,963	267,703	341,232
10. Iowa apportionable income	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
11. Apportionment factor (%) - (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
12. Iowa taxable income	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
13. Tax rate	8%-$2500	8%-$2500	8%-$2500	8%-$2500	10%-$2500
14. Computed tax	121,363	128,098	141,242	144,503	181,762
15. Tax previously paid	(81,466)	(89,001)	(96,072)	(97,921)	(114,618)
16. Additional tax	39,897	39,097	45,170	46,582	67,144
17. Interest to 7-31-74	14,363	11,729	10,841	8,385	8,057
18. Total additional tax & interest	54,260	50,826	56,011	54,967	75,201

EXHIBIT 1-B

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Computation of Assignable Income

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Tax exempt interest	21,245	28,542	28,390	28,305	4,207
Other interest (see below)	335,274	343,827	440,573	239,398	337,025
Total assignable income	356,519	372,369	468,963	267,703	341,232
Other interest	436,157	471,378	598,511	314,991	446,075
Less: Related expense	-0-	(5,992)	(3,384)	(2,787)	(4,422)
Net other interest	436,157	465,386	595,127	312,204	441,653
Less: 50% of federal tax	(100,883)	(121,559)	(154,554)	(72,806)	(104,628)
Net assignable interest	335,274	343,827	440,573	239,398	337,025

EXHIBIT 1-C

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Computation of Sales Factor for Single Factor Formula
(Sales are as Defined Under Iowa Law)

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Gross sales everywhere	97,719,800	118,207,705	135,883,470	151,075,131	143,524,021
Iowa sales as reported	22,102,015	25,988,163	28,157,947	29,794,945	26,797,822
Less: Interstate sales	(721,695)	(912,340)	(1,050,313)	(1,159,547)	N/A
Corrected Iowa sales	21,380,320	25,075,823	27,107,634	28,635,398	26,797,822
Line 5 ÷ line 1 (%)	21.8792	21.2134	19.9492	18.9544	18.6713

EXHIBIT #2

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Computation of Sales Factor for Purposes of 3-Factor,
Weighted 3-Factor, 2-Factor, 2-Factor Modified Formulae
(Sales are as Defined under UDITPA)

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Gross sales everywhere	97,719,800	118,207,705	135,883,470	151,075,131	143,524,021
Iowa sales as reported	22,102,015	25,988,163	28,157,947	29,794,945	26,797,822
Line 17 ÷ line 15 (%)	22.6177	21.9852	20.7221	19.7219	18.6713

EXHIBIT #3

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Property, Payroll & Sales Factors Employed in Comparative Schedules

	3-31-68		3-31-69		3-31-70	
	Total	Iowa	Total	Iowa	Total	Iowa
Tangible Property:						
End of year	24,685,142	1,242,713	25,453,639	1,875,264	28,672,165	2,013,572
Beginning of year	19,567,675	637,240	24,685,142	1,242,713	25,453,639	1,875,264
Total	44,252,817	1,879,953	50,138,781	3,117,977	54,125,804	3,888,836
Average	22,126,409	939,977	25,069,391	1,558,989	27,062,902	1,944,418
Rent expense capitalized (x8)	939,070	-0-	1,619,366	-0-	1,756,783	-0-
Property factors	23,065,479	939,977	26,688,757	1,558,989	28,819,685	1,944,418
Percentage		4.0753		5.8414		6.7468
Payroll:	23,919,381	3,739,426	26,704,658	4,093,875	30,215,738	4,408,774
Percentage		15.6335		15.3302		14.5910
Sales and receipts (exh. #2)	97,719,800	22,102,015	118,207,705	25,988,163	135,883,470	28,157,947
Percentage		22.6177		21.9852		20.7221
Total percentages		42.3265		43.1568		42.0599
Average		14.1088		14.3856		14.0200

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Property, Payroll & Sales Factors Employed in Comparative Schedules

	3-31-71		3-31-72	
	Total	Iowa	Total	Iowa
Tangible property:				
End of Year	40,211,366	2,221,668	44,118,236	2,175,087
Beginning of year	28,672,165	2,013,572	40,211,366	2,221,668
Total	68,883,531	4,235,240	84,329,602	4,396,755
Average	34,441,766	2,117,620	42,164,801	2,198,378
Rent expense capitalized (x8)	1,142,397	-0-	1,106,226	-0-
Property factors	35,584,163	2,117,620	43,271,027	2,198,378
Percentage		5.9510		5.0805
Payroll:	34,307,789	4,797,214	32,302,868	4,183,587
Percentage		13.9829		12.9511
Sales and receipts (exh. #2)	151,075,131	29,794,945	143,524,021	26,797,822
Percentage		19.7219		18.6713
Total percentages		39.6558		36.7029
Average		13.2186		12.2343

EXHIBIT #4

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Computation of Modified 2-Factor (Property + Payroll and Sales)

	3-31-68		3-31-69		3-31-70	
	Total	Iowa	Total	Iowa	Total	Iowa
Property values (exh. #3)	23,065,479	939,977	26,688,757	1,558,989	28,819,685	1,944,418
Payroll	23,919,381	3,739,426	26,704,658	4,093,875	30,215,738	4,408,774
Total	46,984,860	4,679,403	53,393,415	5,652,864	59,035,423	6,353,192
Percentage		9.9594		10.5872		10.7617
Sales and receipts (exh. #2)	97,719,800	22,102,015	118,207,705	25,988,163	135,883,470	28,157,947
Percentage		22.6177		21.9852		20.7221
Total percentages		32.5771		32.5724		31.4838
Average		16.2886		16.2862		15.7419

	3-31-71		3-31-72	
	Total	Iowa	Total	Iowa
Property values (exh. #3)	35,584,163	2,117,620	43,271,027	2,198,378
Payroll	34,307,789	4,797,214	32,302,868	4,183,587
Total	69,891,952	6,914,834	75,573,895	6,381,965
Percentage		9.8936		8.4447
Sales and receipts (exh. #2)	151,075,131	29,794,945	143,524,021	26,797,822
Percentage		19.7219		18.6713
Total percentages		29.6155		27.1160
Average		14.8078		13.5580

EXHIBIT #5

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
2-Factor (Property & Sales)

	3-31-68		3-31-69		3-31-70	
	Total	Iowa	Total	Iowa	Total	Iowa
Property values (exh. #3)	23,065,479	939,977	26,688,757	1,558,989	28,819,685	1,944,418
Percentage		4.0753		5.8414		6.7468
Sales and receipts (exh. #2)	97,719,800	22,102,015	118,207,705	25,988,163	135,883,470	28,157,947
Percentage		22.6177		21.9852		20.7221
Total percentages		26.6930		27.8266		27.4689
Average		13.3465		13.9133		13.7345

	3-31-71		3-31-72	
	Total	Iowa	Total	Iowa
Property values (exh. #3)	35,584,163	2,117,620	43,271,027	2,198,378
Percentage		5.9510		5.0805
Sales and receipts (exh. #2)	151,075,131	29,794,945	143,524,021	26,797,822
Percentage		19.7219		18.6713
Total percentages		25.6729		23.7518
Average		12.8365		11.8759

EXHIBIT #6

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Computation of Weighted 3-Factor Formula of Property, Payroll & Sales
(Weight - 25% Property, 25% Payroll & 50% Sales)

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Property factor percentage (exh. #3)	4.0753	5.8414	6.7468	5.9510	5.0805
Times weight (25%)	x .25	x .25	x .25	x .25	x .25
Weighted percentage	1.0188	1.4604	1.6867	1.4878	1.2701
Payroll factor percentage (exh. #3)	15.6335	15.3302	14.5910	13.9829	12.9511
Times weight (25%)	x .25	x .25	x .25	x .25	x .25
Weighted percentage	3.9084	3.8326	3.6478	3.4957	3.2378
Sales factor percentage (exh. #2)	22.6177	21.9852	20.7221	19.7219	18.6713
Times weight (50%)	x .50	x .50	x .50	x .50	x .50
Weighted percentage	11.3089	10.9926	10.3611	9.8610	9.3357
Total of weighted percentages	16.2361	16.2856	15.6956	14.8445	13.8436

EXHIBIT #7

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Computation of Apportionable Income Without Federal Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Net income per federal	10,393,161	11,682,724	13,949,834	13,528,542	13,394,682
Add: Iowa income tax	30,294	81,466	106,813	80,528	129,054
Interest state & municipal securities	21,244	28,542	28,390	28,305	4,207
	10,444,699	11,792,732	14,085,037	13,637,375	13,527,943
Deduct: Interest federal securities	607,632	673,704	986,187	519,496	144,617
Net income after adjustments	9,837,067	11,119,028	13,098,850	13,117,879	13,383,326
Deduct: Assignable income (see below)	457,402	493,928	623,517	340,509	145,860
Apportionable net income	9,379,665	10,625,100	12,475,333	12,777,370	12,937,466

Computation of Assignable Income

Tax exempt interest	21,245	28,542	28,390	28,305	4,206
Other interest	436,157	471,378	598,511	314,991	446,075
Less: related expense	-0-	(5,992)	(3,384)	(2,787)	(4,422)
Net assignable interest	457,402	493,928	623,517	340,509	445,860

EXHIBIT #8

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Comparative Schedule
Single Factor vs. 3-Factor (Sales, Property & Payroll)
Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with federal tax ded. (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor rate (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
3-Factor rate (exh. #3)	14.1088	14.3856	14.0200	13.2186	12.2343
Income after 3-factor applied	998,411	1,107,038	1,262,742	1,281,477	1,207,367
Difference - greater (less)	(549,873)	(525,431)	(534,027)	(556,056)	(635,248)

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EXHIBIT 9

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Comparative Schedule
Single Factor vs. 3-Factor (Sales, Property & Payroll)
Without Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor rate (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income without fed. tax ded. (exh.#7)	9,379,665	10,625,100	12,475,333	12,777,370	12,937,466
3-Factor rate (exh. #3)	14.1088	14.3856	14.0200	13.2186	12.2343
Income after 3-factor applied	1,323,358	1,528,484	1,749,042	1,688,989	1,582,808
Difference - greater (less)	(224,926)	(103,985)	(47,727)	(148,544)	(259,807)

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EXHIBIT #10

HOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Sales Factor vs. Modified 2-Factor (Property + Payroll and Sales)
Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor rate (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Modified 2-factor rate (exh. #4)	16.2886	16.2862	15.7419	14.8078	13.5580
Income after modified 2-factor applied	1,152,664	1,253,298	1,417,829	1,435,541	1,337,999
Difference - greater (less)	(395,620)	(379,171)	(378,940)	(401,992)	(504,616)

EXHIBIT #11

HOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Comparative Schedule
Sales Factor vs. Modified 2-Factor (Property + Payroll and Sales)
Without Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor rate (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income without fed. tax ded. (exh. #7)	9,379,665	10,625,100	12,475,333	12,777,370	12,937,466
Modified 2-factor rate (exh. #4)	16.2886	16.2862	15.7419	14.8078	13.5580
Income after modified 2-factor applied	1,527,816	1,730,425	1,963,854	1,892,047	1,754,062
Difference - greater (less)	(20,468)	97,956	167,085	54,514	(88,553)

EXHIBIT #12

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Comparative Schedule
Single Factor vs. 2-Factor (Property and Sales)
Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor rate (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
2-factor rate (exh. #5)	13.3465	13.9133	13.7345	12.8365	11.8759
Income after 2-factor applied	944,466	1,070,693	1,237,028	1,244,434	1,171,997
Difference - greater (less)	(603,818)	(561,776)	(559,741)	(593,099)	(670,618)

EXHIBIT #13

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Comparative Schedule
Single Factor vs. 2-Factor (Property and Sales)
Without Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income without fed. tax ded. (exh.#7)	9,379,665	10,625,100	12,475,333	12,777,370	12,937,467
2-factor rate (exh.#5)	13.3465	13.9133	13.7345	12.8365	11.8759
Income after 2-factor applied	1,251,857	1,478,302	1,713,425	1,640,167	1,536,441
Difference - greater (less)	(296,427)	(154,167)	(83,344)	(197,366)	(306,174)

EXHIBIT #14

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Comparative Schedule
Single Factor vs. Weighted 3-Factor (Property 25%, Payroll 25% and Sales 50%)
Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with fed. tax deducted(exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor rate (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Weighted 3-Factor rate (exh. #6)	16.2361	16.2856	15.6956	14.8445	13.8436
Income after weighted 3-factor applied	1,148,949	1,253,252	1,413,659	1,439,099	1,366,184
Difference - greater (less)	(399,335)	(379,217)	(383,110)	(398,434)	(476,431)

EXHIBIT #15

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Comparative Schedule
Single Factor vs. Weighted 3-Factor (Property 25%, Payroll 25% and Sales 50%)
Without Federal Income Tax Deducted

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Apportionable income with fed. tax deducted (exh.#1-A)	7,076,510	7,695,461	9,006,720	9,694,495	9,868,703
Sales factor rate (exh. #1-C)	21.8792	21.2134	19.9492	18.9544	18.6713
Income after sales factor applied	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615
Apportionable income without fed. tax ded. (exh. #7)	9,379,665	10,625,100	12,475,333	12,777,370	12,937,466
Weighted 3-factor rate (exh. #6)	16.2361	16.2856	15.6956	14.8445	13.8436
Income after weighted 3-factor applied	1,522,892	1,730,361	1,958,078	1,896,737	1,791,011
Difference - greater (less)	(25,392)	97,892	161,309	59,204	(51,604)

EXHIBIT #16

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Recapitulation of Alternative Factor Comparisons
"Income Apportioned to Iowa"

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72	Total
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(1) 3-factor (federal tax deducted)	998,411	1,107,038	1,262,742	1,281,477	1,207,367	5,857,035
Alternative - greater (less)	(549,873)	(525,431)	(534,027)	(556,056)	(635,248)	(2,800,635)
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(2) 3-factor (federal tax not deducted)	1,323,358	1,528,484	1,749,042	1,688,989	1,582,800	7,872,681
Alternative - greater (less)	(224,926)	(103,985)	(47,727)	(148,544)	(259,807)	(784,989)
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(3) 2-factor (federal tax deducted)	944,466	1,070,693	1,237,028	1,244,434	1,171,997	5,668,618
Alternative - greater (less)	(603,818)	(561,776)	(559,741)	(593,099)	(670,618)	(2,989,052)
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(4) 2-factor (federal tax not deducted)	1,251,857	1,478,302	1,713,425	1,640,167	1,536,441	7,620,192
Alternative - greater (less)	(296,427)	(154,167)	(83,344)	(197,366)	(306,174)	(1,037,478)
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(5) Modified 2-factor (federal tax deducted)	1,152,664	1,253,298	1,417,829	1,435,541	1,337,999	6,597,331
Alternative - greater (less)	(395,620)	(379,171)	(378,940)	(401,992)	(504,616)	(2,060,339)
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(6) Modified 2-factor (federal tax not deducted)	1,527,816	1,730,425	1,963,854	1,892,047	1,754,062	8,868,204
Alternative - greater (less)	(20,468)	97,956	167,085	54,514	(88,553)	210,534
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(7) Weighted 3-factor (federal tax deducted)	1,148,949	1,253,252	1,413,659	1,439,099	1,366,184	6,621,143
Alternative - greater (less)	(399,335)	(379,217)	(383,110)	(398,434)	(476,431)	(2,036,527)
Single factor (federal tax deducted)	1,548,284	1,632,469	1,796,769	1,837,533	1,842,615	8,657,670
(8) Weighted 3-factor (federal tax not deducted)	1,522,892	1,730,361	1,958,078	1,896,737	1,791,011	8,899,079
Alternative - greater (less)	(25,392)	97,892	161,309	59,204	(51,604)	241,409

EXHIBIT #17

MOORMAN MANUFACTURING COMPANY
3-31-68 THROUGH 3-31-72
Percentage of Income Apportioned to Iowa Compared to Total Apportionable Income After Deduction For Federal Income Taxes

	3-31-68	3-31-69	3-31-70	3-31-71	3-31-72
Single factor (federal tax deducted)	21.8792	21.2134	19.9492	18.9544	18.6713
(1) 3-factor (federal tax deducted)	14.1088	14.3856	14.0200	13.2186	12.2343
(2) 3-factor (federal tax not deducted)	18.7007	19.8621	19.4193	17.4221	16.0387
(3) 2-factor (federal tax deducted)	13.3465	13.9133	13.7345	12.8365	11.8759
(4) 2-factor (federal tax not deducted)	17.6903	19.2101	19.0239	16.9185	15.5688
(5) Modified 2-factor (federal tax deducted)	16.2886	16.2862	15.7419	14.8078	13.5580
(6) Modified 2-factor (federal tax not deducted)	21.5900	22.4863	21.8043	19.5167	17.7740
(7) Weighted 3-factor (federal tax deducted)	16.2361	16.2856	15.6956	14.8445	13.8436
(8) Weighted 3-factor (federal tax not deducted)	21.5204	22.4855	21.7402	19.5651	18.1484

(EXHIBIT 14)

MOORMAN MANUFACTURING COMPANY
Sales

	FYE 3-31-68	FYE 3-31-69	FYE 3-31-70	FYE 3-31-71	FYE 3-31-72
Total Sales	$97,719,800	$118,207,705	$135,883,470	$151,075,131	$143,524,021
Iowa Sales	21,380,320	25,075,823	27,107,634	28,635,398	26,797,822
Illinois Sales	16,615,504	18,280,667	21,138,611	22,624,369	20,390,363

(EXHIBIT 15)

MOORMAN MANUFACTURING COMPANY
Payroll

	FYE 3-31-68	FYE 3-31-69	FYE 3-31-70	FYE 3-31-71	FYE 3-31-72
Total Payroll	$23,919,381	$26,704,658	$30,215,738	$34,307,789	$32,302,868
Iowa Payroll	3,739,426	4,093,875	4,408,774	4,797,214	4,183,587
Illinois Payroll	9,805,869	10,891,112	12,437,449	14,015,400	13,203,352

(EXHIBIT 16)

MOORMAN MANUFACTURING COMPANY
Property

	FYE 3-31-68	FYE 3-31-69	FYE 3-31-70	FYE 3-31-71	FYE 3-31-72
Total Property	$21,501,087	$22,606,825	$30,785,276	$38,905,786	$44,909,979
Iowa Property	1,133,303	1,457,801	1,947,995	2,117,620	2,243,153
Illinois Property	18,123,442	18,945,268	19,082,308	24,386,873	31,506,000

EXHIBIT 17

ANALYSIS OF IOWA CORPORATION INCOME RETURNS
OF NON-IOWA MANUFACTURERS FOR THE PERIOD
1964-1972

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	No. of Returns Filed	No. of Returns Filed on Other Than Single Factor	No. of Returns Where 3 Factor Allowed	No. Where 3 Factor Disallowed	No. Where Weighted Factor Disallowed	No. Where Three Factor Allowed by Statute of Limitation	No. Where Weighted Factor Allowed by Statute of Limitation
964	263	14	2	9	0	2	1
965	277	14	2	10	1	0	1
966	304	16		11	1	3	1
967	325	14		8	1	4	1
968	344	17		14	1	2	0
969	358	17	1	15	1	0	0
970	389	17		15	0	1	0
971	422	23		23	1	0	0
972	456	17		17	0	0	0

IN THE DISTRICT COURT OF THE STATE OF IOWA
In and for Polk County

EQUITY NO. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Defendant.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

(Filed December 17, 1976)

NOW on this 17 day of December, 1976, the above captioned cause coming on for trial before the undersigned on the 19th day of August, 1976, the plaintiff Moorman Manufacturing Company represented by Walter R. Brown and John V. Donnelly; the defendant G. D. Bair, as Director of Revenue for the State of Iowa, represented by Harry M. Griger, Assistant Attorney General; and appearing as amicus curiae by special leave of Court is the Iowa Manufacturers Association represented by James L. Rogers, John R. Phillips, and Russell L. Samson; the Court finds it has jurisdiction over the subject matter of this action and the parties hereto, and having heard legal arguments in this matter, having studied the stipulation of facts agreed between parties to be the evidence submitted, having carefully examined the extensive support provided for respective positions by briefs, after long and careful reflection, is now prepared to rule.

This action, putting squarely at issue the constitutionality of Iowa Code Section 422.33, finds its genesis in the defendant's December 17, 1974 order revising and adjusting Moorman's income tax assessment for that corporation's fiscal years of operation ending March 31, 1968 through March 31, 1972. The amount put in issue by that assessment, taxes and interest, totals $321,628.95. Moorman has taken appeal from the defendant's order affirming the revised and adjusted assessment by the provisions of Iowa Code Section 422.29 (1971) which cast this matter before the Court on a *de novo* basis. Because this cause has been submitted on an agreed stipulation of facts, no evidence beyond that in the stipulation was presented or is considered and as the parties to this action have requested by Paragraph 35 of said stipulation, this opinion merely makes findings of fact and conclusions of law but withholds the decretal or judgmental portion of this opinion upon which an appeal can immediately result.

PRELIMINARY FINDINGS OF FACT

The plaintiff, Moorman Manufacturing Company (hereinafter Moorman) is a corporation organized and existing under the laws of the State of Illinois and doing business in Iowa as well as several other states. For the period in question and currently, Moorman's principal source of income was generated by the manufacture and sale of more than eighty different products for feeding livestock and poultry with the greatest portion of those sales centered about the sale of mineral and protein supplements for livestock. Moorman's holdings are as extensive as they are scattered. It owns all of the outstanding stock of Quincy Soybean Co., Quincy, Illinois; the Moorman Manufacturing Company of California, Inc., San Gabriel, California; and Bell Grain and Milling, Inc., of Perris, California. Bell, in turn, owns all the outstand-

ing stock of Bell Milling Corporation of Escondido, California. Moorman's manufacturing facilities are located in five separate plants in three states: Quincy, Illinois; Alpha, Illinois; Comanche, Texas; Hereford, Texas, and Columbus, Nebraska. None of Moorman's manufacture occurs in Iowa. Moorman's products are principally sold directly to farmers and ranchers by its sales force of more than 2,500 salesmen, all paid on a commission basis, in more than thirty states of this country.

During the years in issue, March, 1968 through March, 1972, Moorman conducted a continuous solicitation and sales campaign to potential Iowa customers by its sales force of between 518 and 582 Iowa salesmen and warehousemen. Resulting sales were satisfied by delivery of its product from one to six warehouses in Iowa, located in Stanwood, Plainfield, Goldfield, Marcus, Atlantic, and Knoxville. The products sold in Iowa and delivered from one of the above distribution points were manufactured exclusively by Moorman's Illinois plants.

Due to its widely disbursed business activities Moorman pays income taxes to a number of states in addition to Iowa. It operates, for tax purposes, on a fiscal year basis ending March 31 of each year. Moorman's Iowa income tax returns for fiscal years ending March 31, 1968, 1969, 1970, 1971, and 1972 were all timely filed as required by statute and while the method of computation employed by it did not conform to the requirements of Iowa Code Section 422.33(1), the method used by Moorman was clearly disclosed on its returns for those years. Indeed, Exhibits 1 through 5 relating respectively to tax years March 31, 1968 through March 31, 1972, identify precisely the factors Moorman used to compute its Iowa taxes and cited as authority for so doing "General Motors Corp. v. D.C. U.S. Supreme Court Docket No. 352".

On December 22, 1972, D. G. Brigg's, defendant Bair's predecessor in office, issued an Income Tax Assessment Notice against Moorman relating to plaintiff's tax returns for its fiscal years of 1968 through 1972. That assessment found taxes and interest due from plaintiff respecting those fiscal years in the amount of $321,628.95, since Moorman had chosen to compute its taxes on the basis of a three factor formula and not the single factor sales formula of Iowa Code Section 422.33(1). Plaintiff's appeal from that assessment resulted in a hearing conducted before defendant on October 24, 1974. As mentioned above, it was defendant's December 17, 1974 order affirming the revised assessments which led to the appeal taken here.

The history of Moorman's tax intercourse with Iowa dates back to 1949 when it filed its first income tax return for fiscal year ending March 31, 1949. With approval of the Iowa State Tax Commission, Moorman, after allocating its interest, dividends, rents, and royalties, less expenses related thereto, apportioned the remainder of its net income to the State of Iowa on the ratio that its payroll, property, and sales within Iowa bore to its payroll, property, and sales everywhere through its operations in the United States, giving equal weight (.33) to each element in the ratio. This method of computation was followed for each year from 1949 to March 31, 1960. But at the direction of the State Tax Commission, Moorman computed its income tax obligation for the fiscal years of 1961 through and including 1965 by adherence to the single sales factor formula of Iowa Code Section 422.33(1). Beginning in its fiscal year of 1965, however, Moorman again applied the equally balanced three-factor—property-payroll-sales formula to its income thereafter. To this application of the three factor formula the State Tax Commission did not consent. It was the result of Moorman's

use for its fiscal years of 1968 through 1972 inclusive of the three factor formula that the December 22, 1972 notice of income tax assessment found additional amounts of tax due when recomputation conformed to the single sales factor tax formula of Iowa Code Section 422.33(1).

Based upon the facts submitted, more of which will be discussed in connection with each separately considered legal argument, the parties have presented several questions of law. Classified broadly and in the order in which such questions will be addressed below, we must determine (1) whether the statute of limitations in Iowa Code Section 422.25 defeats recovery by defendant of that portion of its revised assessment respecting Moorman's income for the fiscal years of 1968 and 1969; (2) whether the single sales factor formula of Iowa Code Section 422.33 is facially unconstitutional as in violation of the due process or equal protection clauses of the Fourteenth Amendment to the United States Constitution and the same provisions of the Iowa Constitution and in violation of the Commerce Clause of the Federal Constitution; (3) whether, depending upon the conclusions made concerning facial unconstitutionality, the single sales factor formula of our Code is unconstitutional as applied to Moorman as in violation of the same constitutional injunctions.

We turn to the problems posed by the statute of limitations in Iowa Code Section 422.25.

STATUTE OF LIMITATIONS

Iowa Code Section 422.25 reads, *inter alia*,

> "*Computation of tax, interest, and penalties—limitation.*
>
> "1. As soon as practicable and in any event within three years after the return is filed the department shall examine it and determine the correct amount of tax, and the amount so determined by the department shall be the tax; . . . Notwithstanding the periods of limitation for examination and determination heretofore specified, the department shall have six months from the date of final disposition of any controversy between the taxpayer and the internal revenue service with respect to the particular tax year to make the examination and determination."

Of the $321,628.95 the defendant assessed in arrearages by its Income Tax Assessment Notice of December 22, 1972, $62,073.77 is attributable to the defendant's revised assessment for Moorman's fiscal year ending March 31, 1968, and $59,272.03 represents the defendant's increased assessment for Moorman's tax year of 1969.

As noted above, Moorman timely filed its Iowa income tax returns for 1968 and 1969 indicating clearly, although not with defendant's consent, the apportionment formula it applied to income for those years.

Thus the three year statute of limitations in Section 422.25, unaffected by willful omissions or fraud considerations that would bring to bear either a six year or unlimited limitation period, began to run July 31, 1968 and July 31, 1969, and expired July 31, 1971, and July 31, 1972, respectively. Since the Notice of Income Tax Assessment bears the date December 22, 1972, the revised assessment respecting 1968 and 1969 would seem clearly to be uncollectible as beyond the limitation period. The catch is that Moorman's federal income tax returns were the subject of an audit by the United States Internal Revenue Service beginning in June, 1970 which called into question its returns for its fiscal years of 1968 and 1969. The audits were concluded by a written agreement between Moorman and the I.R.S. on or about October

8, 1973. The audit and agreement however resulted in no change which would affect the determination of how Moorman's net income arising from the sale of tangible personal property should be apportioned to the State of Iowa, whether by application of the statutory single sales factor apportionment method or by the three factor formula used by Moorman.

Although the audit and agreement respecting Moorman's income for those years made no difference in its income for Iowa's taxing purposes, by virtue of the federal inquiry the defendant contends the basic three year limitation period no longer applies because the revised assessment for 1968 and 1969 came well before "six months from the date of final disposition of any controversy between the taxpayer and internal revenue service with respect to the particular tax year. . . ." Section 422.25(1), The Code. Acknowledging that the audit produced no results upon which a change might follow in Iowa tax due, the defendant concedes that the audit by the I.R.S. is the only basis for its argument that the general three year limitation does not apply.

It is clear, as Moorman observes, that purpose of extending the primary three year limitation in Section 422.25 six months from the final disposition of any controversy between a taxpayer and the federal internal revenue service, is to allow the state to take advantage of the auditing efforts conducted under federal auspices.

While we believe the director would be remiss in his duties by failing to make "an examination and determination" of tax returns in the three year limitation period all the while awaiting possible institution of similar efforts by the Internal Revenue Service, the six months exception to the three year bar is neatly tailored to allow Iowa tax officials another opportunity in scrutinizing corporate

returns when federal examination of that taxpayer's returns results in adjustments which might present grounds for similar changes in Iowa tax liabilities.

Of course, the case here presents an added difficulty. If the federal audit discloses no information by which Iowa may make additional assessments, does the mere fact a federal audit took place leave the defendant a foothold for making a revised and adjusted assessment, otherwise barred by the limitation prohibition, and allowing him to recompute the corporate taxpayer's liability on the basis of taxing formula criteria different than the taxpayer disclosed in its returns?

We return to the statute for a more careful reading of the words our legislature chose to manifest its intent.

The duty of the department, to be accomplished "as soon as practicable and in any event within three years" from the filing of a corporate taxpayer's returns, is to 'examine' the returns and 'determine' the correct amount of tax. Section 422.25. Notwithstanding this general limitation, the department is given an additional six months which begins upon the resolution of a controversy existing between the taxpayer and Internal Revenue Service to 'examine and determine' the taxpayer's Iowa returns in light of the final disposition made between the taxpayer and Internal Revenue Service. During either the first three year period or a second six months extension, the scope of the department's inquiry respecting the taxpayer's returns is the same—the department must 'examine' and 'determine'.

Webster's Seventh New Collegiate Dictionary 288-9 (1965) defines the verb 'examine' to mean "to inspect closely; to test the condition of; to inquire into carefully. . . ." 'Determine', as a verb, is defined to include the

following actions: "to fix conclusively or authoritatively; to decide by judicial sentence; to settle or decide by choice of alternatives or possibilities; . . . to come to a decision. . . ." *Id.*, at 226.

Because the legislature gave the department the same latitude in reviewing a taxpayer's returns after a federal audit had begun as the department had initially within the original three year examination period, the conclusion would seem inescapable that the department is not limited to a mere *recomputation* of the taxpayer's Iowa liability based upon newly developed federal figures (emphasis added). The department is accorded the authority, as they are in the first instance, to scrutinize and inspect the Iowa returns and decide and fix the amount of tax liability. Thus it is apparent that the department may challenge Moorman's apportionment formula and the tax liability following from its use in the period beyond the three year limitation as within its powers to both 'examine and determine'.

More supportive still of this conclusion is a focus on another aspect of the six months statutory exception. Regarding the nature of the controversy existing between the taxpayer and Internal Revenue Service, Section 422.25 says ". . . the department shall have six months from the date of final disposition of *any* controversy between the taxpayer and the internal revenue service. . . ." (emphasis added).

We cannot help but believe that the broad powers vested in the department to 'examine and determine' anew after a federal audit had begun were powers then constrained to such duties only if the federal audit produced adjusted income which, in turn, might adjust Iowa taxable income. It is plain that the controversies between the

taxpayer and Internal Revenue Service which can result in application of the department's statutory duties are not just certain controversies whose resolution changes the taxpayer's base for Iowa tax purposes but "any controversy" whether a change affecting Iowa tax results or does not result.

In sum, this Court concludes that the defendant properly made his revised assessment using the statutory formula of Section 422.33 on income attributable to Moorman's fiscal tax years ending March 31, 1968 and 1969.

We turn now to the more onerous task of determining the constitutionality of the 'single factor sales' formula of Section 422.33.

CONSTITUTIONALITY

It is necessary at the outset to review the standards by which the constitutionality of legislation is measured. The principles are well known that

> "(r)egularly enacted statutes are accorded a strong presumption of constitutionality. When constitutionality is merely doubtful [courts] will not interfere as it must be shown that legislative enactments clearly, palpably and without doubt infringe upon constitutional rights before an attack will be upheld. Every reasonable basis of support for a statute must be negated by the attacking party."

State v. *Aldrich*, 231 N.W.2d 890, 894 (Iowa 1975) (quoting, *State* v. *Kueny*, 215 N.W.2d 215 (Iowa 1974)); *Lee Enterprises, Inc.* v. *Iowa State Tax Commission*, 162 N.W.2d 730 (Iowa 1968); *Vilas* v. *Iowa State Board of Assessment and Review*, 223 Iowa 604, 273 N.W. 338 (1937); *Cook* v. *Hannah*, 230 Iowa 249, 297 N.W. 262 (1941).

The burden falls upon the party challenging the statute's constitutionality to negative every reasonable basis upon which the statute might be sustained. *State* v. *Hall*, 227 N.W.2d 192, 193 (Iowa 1975); *Green* v. *Shama*, 217 N.W.2d 547 (Iowa 1974); *Keasling* v. *Thompson*, 217 N.W.2d 687 (Iowa 1974); *Lee Enterprises, supra*, at 238. 84 C.J.S. *Taxation* Section 36 at 121 (1954) ("(t)he presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons or classes.")

In the field of taxation, perhaps more than in any other area, legislatures are accorded the greatest deference in constructing workable taxing mechanisms. *Lehnhausen* v. *Lake Shore Auto Parts Co.*, 410 U.S. 356 (1973). In *Madden* v. *Commonwealth of Kentucky*, 309 U.S. 83, 87-8 (1939) the United States Supreme Court observed:

> "The broad discretion as to classification possessed by a legislature in the field of taxation has long been recognized. This Court fifty years ago concluded that 'the fourteenth amendment was not intended to compel the states to adopt an iron rule of equal taxation,' and the passage of time has only served to underscore the wisdom of that recognition of the large area of discretion which is needed by a legislature in formulating sound tax policies. Traditionally classification has been a device for fitting tax programs to local needs and usages in order to achieve an equitable distribution of the tax burden. It has, because of this, been pointed out that in taxation even more than in other fields, legislatures possess the greatest freedom in classification. Since the members of a legislature necessarily enjoy a familiarity with local conditions which this Court cannot have, the presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is hostile and oppressive discrimination against particular persons and classes. The burden is on the one attacking the legislature arrangement to negative every conceivable basis which might support it." (numerous footnotes omitted).

Mindful as we are of the very delicate and sensitive obligations which we now undertake and fully aware of all presumptions and burdens which run in favor of a declaration of constitutionality of the legislation now at issue, we assume the duty that is ours and turn to the constitutional attack levied by Moorman against Iowa Code Section 422.33. *Marbury* v. *Madison*, 1 (Cranch) 427 (1804).

FACIAL CONSTITUTIONALITY OF SECTION 422.33

Iowa Code Section 422.33 reads:

> *"Corporate tax imposed.* A tax is hereby imposed upon each corporation organized under the laws of this state, and upon every foreign corporation doing business in this state, annually in an amount computed by applying the following rates of taxation to the net income received by the corporation during the income year:
>
> [rates omitted]
>
> "1. If the trade of business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on the portion of the net income reasonably attributable to the trade or business within the state, said net

income attributable to the state to be determined as follows:

"a. Interest, dividends, rents and royalties (less related expenses) received in connection with business in the state, shall be allocated to the state, and where received in connection with business outside the state, shall be allocated outside the state.

"b. Net income of the above class having been separately allocated and deducted as above provided, the remainder of the net income of the taxpayer shall be allocated and apportioned as follows:

. . . .

"Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

"The gross sales of the corporation within the state shall be taken to be the gross sales from goods sold and delivered within the state, excluding deliveries for transportation out of the state."

Iowa Code Section 422.33 taxes corporate net income from the manufacture and sale of tangible personal property using an apportionment method applied to corporations doing business both in the state and out of the state on that portion of net income the statute says is "reasonably attributable" to the business conducted in state. The method described for 'reasonably attributing' net income as between in-state and extra-territorial activity is the fraction defined by manufacturers' in-state sales of tangible personal property, as the numerator, over similar sales of such property made by that manufacturer everywhere

else—the denominator. The resulting fraction is applied to the manufacturer's net income and the result is the income taxable in Iowa. This taxing method is commonly referred to as the 'single-factor sales formula'.

By contrast and for a full understanding of the operation of the single factor sales formula, the apportionment method Moorman employed when filing its tax returns for the years in question is commonly known as the three factor formula. That formula in its operation employs not only sales in Iowa as an indicia of the tax it should pay here but includes two other factors: the payroll of its Iowa personnel and the value of the manufacturer's in-state property holdings. Taking, as an example, then, Moorman's business for its fiscal year ending March 31, 1968, the results in application of the Iowa single sales factor formula and the three factors (sales, payroll, property) formula are seen to produce readily apparent differences in the tax Moorman must pay this state.

For Moorman's fiscal year 1968, it reported total gross sales from all of its operations in this country of $97,719,800. Of that sum, $22,102,015 represented sales in Iowa. Application of the single factor formula results in the fraction of approximately 1/5—as a percentage, 22.6177%. This factor is multiplied against Moorman's net income with the product representing the taxable income to which Iowa applies its rates.

The three factor approach used instead by Moorman works this way: the Iowa sales percentage (22.6177%) is given one-third weight (.33 x 22.6177%), as are the elements of payroll and property. Moorman's Iowa property holdings for that year represent merely 1/25 of the property it owned everywhere—4.0753%. Moorman's payroll for that year amounted to $23,919,381 of which $3,-

739,426 was paid to its Iowa salesmen and warehousemen. As a fraction between 1/6 and 1/7 of its entire year's payroll went to Iowa wage earners—15.6335%. The property factor and payroll factor are given equal weight with the sales factor so that the weighted percentage applied to Moorman's net income for that year is: (.33 x .226177) + (.33 x .40753) + (.33 x .156335) or .141088, or 14.1088%. This decimal contrasts sharply with the product gained from the single sales factor alone; here .226177.

When these respective products are applied against Moorman's net income for the fiscal year of 1968, the determination would yield—as should readily be clear—Iowa taxable income of $1,548,284 and not the $998,411 which would follow from applying the evenly weighted three factor product. The difference between the formulae applied result in a difference to Iowa of some $549,873 of taxable income and to Moorman in many thousands of dollars in additional tax liability.

These figures show roughly the contrast between the apportionment mechanism Moorman used from 1968 through 1972 and the one later applied by the defendant. Against this backdrop we proceed to the individual constitutional arguments Moorman makes.

EQUAL PROTECTION

Moorman assails the single sales factor tax apportionment method as in violation of the equal protection clause of the Fourteenth Amendment to the United States Constitution and the similar clause in the Iowa Constitution, Article I, Section 6. It contends the classifications established by Section 422.33 invidiously discriminate against it and in favor of solely Iowa based manufacturers who ship most or all of their goods out of state since all of

plaintiff's sales in state are taxed at 100% and those of hypothetical Iowa manufacturers who ship totally out-of-state are not taxed in Iowa at all.

When constitutional provisions of both the federal Constitution and Iowa Constitution contain a similar guarantee, "they are usually deemed to be identical in scope, import and purpose", and cases interpreting the federal standard are consulted "for such light and guidance as they may afford." *Davenport Water Company* v. *Iowa State Commerce Commission,* 190 N.W.2d 583, 593 (Iowa 1971).

In determining whether legislative treatment of various objects sought to be addressed within a statutory scheme violates equal protection, the United States Supreme Court has said:

> " '1. The equal protection clause of the Fourteenth Amendment does not take from the State the power to classify in the adoption of police laws, but admits of the exercise of a wide scope of discretion in that regard, and avoids what is done only when it is without any reasonable basis and therefore is purely arbitrary. 2. A classification having some reasonable basis does not offend against that clause merely because it is not made with mathematical nicety or because in practice it results in some inequality.' " *Morey* v. *Doud,* 354 U.S. 457 (1957) (citing *Lindsey* v. *Natural Carbonic Gas Co.,* 220 U.S. 61 (1911)).

We look to the statute to determine the nature of classifications it prescribes.

Section 422.33, The Code, imposes a tax "upon each corporation organized under the laws of this state, and

upon every foreign corporation doing business in this state. . . ."

It is readily apparent that the statute in question focuses on the classification of 'corporations'. Since classifying corporations for different tax treatment than individual persons has most recently been sustained in *Lehnhausen* v. *Lake Shore Auto Parts Co.*, 410 U.S. 356 (1973), the Iowa scheme taxing corporations cannot be challenged merely because corporations are taxed. Nor does the fact that Section 422.33 establishes a graduated tax on corporate incomes lead to a finding of an invidious classification, for all corporations, without regard to any other factors, have been taxed by the same apportionment mechanism—the single sales factor. See *Illinois Central Ry. Co.* v. *Minnesota*, 309 U.S. 157 (1940). The simple matter is that for purposes of classification, the legislature has singled out the income of all "corporations" as the basis on which the single sales factor is to apply; and while application of the formula yields differing amounts of tax due, for equal protection analysis, all corporations are similarly situated and are accorded exactly the same tax treatment.

This Court concludes that Iowa Code Section 422.33 on its face creates no classifications which may be found to violate Moorman's rights to equal protection of the law under either the Fourteenth Amendment of the United States Constitution or Article I, Section 6 of the Iowa Constitution. Indeed, Moorman's complaints concerning the operation of Section 422.33 would seem to be complaints shared by all corporations taxed by the statute whose operations are multi-state in extent. To that end Moorman's next attack is premised on the due process clauses of both Iowa and United States Constitutions.

DUE PROCESS

In approaching Moorman's due process assignments we are haunted by the unquieted spirit of *Lochner* v. *State of New York*, 198 U.S. 45 (1905). It is remarked that if we find the single sales factor statute unconstitutional, our judgment should address which of the myriad of tax formulae currently in use should be that Iowa is left to follow. If it is decided the present statute is unconstitutional, we are petitioned to point the way our taxing systems should be written.

We decline this invitation as it has been rejected so many times before (*West Coast Hotel Co.* v. *Parrish*, 300 U.S. 379 (1937); *Olsen* v. *State of Nebraska*, 313 U.S. 236 (1941); *Lincoln Federal Labor Union* v. *Northwestern Co.*, 335 U.S. 525 (1949); *Giboney* v. *Empire Storage Co.*, 336 U.S. 490 (1950); *Williamson* v. *Lee Optical Co.*, 348 U.S. 483 (1955)) and note that this Court is not ordained to sit as the "super legislature" of a prior era in testing the ". . . wisdom, need, and propriety of laws that touch economic problems, business affairs, or social conditions." *Griswold* v. *State of Connecticut*, 381 U.S. 484 (1965); *City National Bank of Clinton* v. *Iowa State Tax Commission*, 251 Iowa 603, 102 N.W.2d 381 (1960); 51 Am. Jur. *Taxation* Section 47 (1944). We determine only whether Section 422.33 is unconstitutional.

In subjecting Moorman's arguments to due process scrutiny the initial inquiry must be whether "the taxing power exerted by the state bears a relation to protection, opportunities and benefits given by the state. The simple but controlling question is whether the state has given anything for which it can ask return." *State of Wisconsin* v. *J. C. Penney Co.*, 311 U.S. 435, 444 (1940). As said in *Northwestern States Portland Cement Company* v. *State*

of *Minnesota*, 358 U.S. 450, 464-5 (1959) denying plaintiff's 'due process' attack,

> "The taxes [there] imposed are levied only on that portion of the taxpayer's net income which arises from its activities within the taxing state. These activities form a sufficient 'nexus between such a tax and transactions within a state for which the tax is an exaction.' *State of Wisconsin* v. *J. C. Penney Co.*, [supra]. It strains reality to say, in terms of our decisions, that each of the corporations here was not sufficiently involved in local events to forge 'some definite link, some minimum connection' sufficient to satisfy due process requirements."

See also *General Motors Corporation* v. *State of Washington*, 377 U.S. 436 (1964); 51 Am. Jur. *Taxation* Section 92 (1944).

Of course, Moorman, first and foremost, is accorded the not invaluable right to do business in the State of Iowa. The record shows its sales in Iowa are substantial. It is given the protection of Iowa laws with resort to the Iowa court system if it determines court powers are needed to protect its corporate rights—as here. It is certain that Moorman's business presence and activities in Iowa with this State's consent constitute the "minimum connection" by which Iowa can constitutionally levy a corporate tax.

The more narrow question presented, however, acknowledging that ". . . the tax in practical operation has relation to opportunities benefits [and] protection conferred or afforded by [Iowa is whether] the tax is fairly apportioned to the commerce carried on within [this State]." *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission*, 390 U.S. 317, 325 (1968) (fn. 5).

Said further by the *Norfolk & Western Railway* Court, addressing a Missouri *ad valorem* tax on railroad rolling stock

> "In some cases the Court has concluded that States have, in fact, cast their tax burden upon property located beyond their borders. [citing cases] The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due.[5] A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to 'project the taxing power of the state plainly beyond its borders.' [cited case] Any formula used must bear a rational relationship, both on its face and in its application, to property values connected with the taxing State."

We return to the facts of Moorman's tax predicament to determine whether the State of Iowa imposes its tax on activities fairly apportioned to Moorman's presence here or whether the single sales factor tax demands more than this State can rightfully ask.

It is useful at this point to remember that while Moorman's sales in Iowa constitute roughly one-fifth of its total interstate sales, all of the goods sold in Iowa are manufactured in Illinois. Taking Moorman's fiscal tax year of 1968 again, Moorman contends, respecting the Illinois manufactured goods sold here, that the Iowa tax recognizes none of the manufacturing inputs (payroll and property) of the Illinois process and taxes only the final end and *raison d'etre* of its production efforts; e.g. sales. Thus Moorman asserts that factors, at least as valuable as sales

used in determining the proportion of taxes it should pay to this State, are left entirely out of the Iowa tax equation. It submits this documentation: For its fiscal year of 1968 the percentage of Moorman's payroll associated with its Illinois operations was 41% of its payroll everywhere; the Iowa payroll percentage was 15.63%. Of its property everywhere, that located in Illinois represented 84.29%, while that in Iowa was a mere 5.27%. Finally its sales in Iowa for that year were 21.88% of its sales everywhere. Yet in light of Moorman's relatively small property holdings and payroll contributions in Iowa (none of which are attributable to the manufacture of goods sold here), this State taxes 100 percent of in-state sales (21.88% of income for 1968), which are to a greatest degree attributable to Illinois plant and personnel inputs. Put slightly different, considering total Iowa and Illinois property and payroll alone, Iowa payroll represents but 27.61% while Illinois payroll, substantially higher, runs at 72.39% of total payroll between these two states. Illinois property predominates in balance with 94.11% located here as between it and this state; Iowa property remains only a miniscule 5.89%. But because the Iowa single sales factor tax admits of neither the property nor payroll inputs of Illinois plant and labor as part of its formula, each dollar in sales of Moorman's goods in Iowa is taxed at 100% while nearly 75% of Moorman's payroll and 30% of its capital is used in the manufacture of the goods taxed here.

While accepting the right of Iowa to tax its corporate income for the services this State renders, it maintains that Iowa cannot tax *all* of Moorman's income because only a small proportion of servicing inputs arise from its relation with this State. Since the largest quantum of capital and labor respecting its product sold here results

from its Illinois relationship, the Iowa apportionment formula fails to reasonably apportion profits traceable to Illinois operations and taxes those activities occurring in Illinois. In this sense, says Moorman, the single sales factor taxes more than that which should be fairly apportioned to Iowa and, as a consequence, violates its constitutional rights of due process under both United States and Iowa Constitutions.

We agree.

Perhaps the closest to confirmation of the holding here reached comes from *General Motors Corporation* v. *District of Columbia*, 380 U.S. 553 (1965). At issue there was a regulation formulated by the Tax Commissioners of District of Columbia pursuant to the District of Columbia Income and Franchise Tax Act of 1947. The statute provided that "(t)he measure of the franchise tax shall be that portion of the net income of the corporation . . . as is fairly attributable to any trade or business carried on or engaged in within the District and such other net income as is derived from sources within the District." The Commissioner's regulation, however, taxed income from the sale of tangible personalty for any particular year on the basis of a single sales factor, which operated in the same manner as Iowa's formula. In striking the regulation as exceeding the statutory authorization permitting a tax only on income "fairly attributable" to the District of Columbia, the Supreme Court left no doubt that the single sales factor apportionment method transgressed more than the statute at issue. Through the discriminating use of dicta, that Court marked the single sales factor formula as potentially violative of constitutional guarantees, although stating they took no position as to the constitutionality of a state tax scheme premised on the use of the single sales factor alone. *Id.*, at 561.

While the constitutional implications of that decision extend more to problems associated with violation of the Commerce Clause (of which more later), so far as 'due process' is here concerned, the Court commented:

> "The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporations income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves." *Id.*, at 559-60.

The plaintiff in that case, General Motors Corporation, stood in exactly the same position as plaintiff here. General Motors' sales in the District of its automobiles were in the millions of dollars and the District tax was imposed upon 100% of such sales. The manufacturing process in that case however, like here, was conducted totally outside the District. The concern the *General Motors* court had with the use of the single sales factor formula was that of the reasonableness of apportionment. Speaking more to Commerce Clause issues, the Court made clear that taxing schemes must fairly apportion corporate incomes so that multiple taxation does not result, as we have found it does in this case.

Finding that Iowa Code Section 422.33 imposes taxes on business activity carried on outside Iowa borders, and therefore violates 'due process', we move on to consider the Commerce Clause assignments.

COMMERCE CLAUSE

In *Northwestern States Portland Cement Company* v. *State of Minnesota*, 358 U.S. 450 (1959) the Supreme Court was called upon to determine the constitutionality of state net income tax laws which levied taxes on that portion of an out-of-state corporation's net income earned in and fairly apportioned to business activity in the forum state. The attack made centered on 'commerce clause' and 'due process' questions. Reviewing the appropriate 'commerce clause' standards the Court detailed:

> "It has long been established doctrine that the Commerce Clause gives exclusive power to the Congress to regulate interstate commerce, and its failure to act on the subject in the area of taxation nevertheless requires that interstate commerce shall be free from any direct restrictions or impositions by the States. Gibbons v. Ogden, 1824, 9 Wheat. 1, 6 L.Ed. 23. In keeping therewith a State 'cannot impose taxes upon persons passing through the state, or coming into it, merely for a temporary purpose' such as itinerant drummers. [case cited]. Moreover, it is beyond dispute that a State may not lay a tax on the 'privilege' of engaging in interstate commerce [case cited]. Nor may a State impose a tax which discriminates against interstate commerce either by providing a direct commercial advantage to local business [cases cited], or by subjecting interstate commerce to the burden of 'multiple taxation' [cases cited]. Such impositions have been stricken because the States, under the Commerce Clause, are not allowed 'one single tax-worth of direct interference with the free flow of commerce.' [case cited]." *Id.*, at 458.

For many intents and purposes, the test of a state's taxing law for Commerce Clause analysis is the same as it is for 'due process' purposes. Thus, as said in *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission, supra,*

> "The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due.[5]
>
> • • •
>
> [fn. 5] We have said: "The problem under the Commerce Clause is to determine 'what portion of an interstate organism may appropriately be attributed to each of the various states in which it functions.' . . . . So far as due process is concerned the only question is whether the tax in practical operation has relation to opportunities, benefits, or protection conferred or afforded by the taxing State." 390 U.S., at 325.

Consideration of these Commerce Clause strictures requires, as it did with 'due process' investigation, that the Iowa single sale factor apportionment method be shown that its application ". . . has resulted in such gross overreaching, beyond the values represented by the intrastate [activity] purported to be taxed, as to violate the Due Process and Commerce Clauses of the Constitution." *Id.*, at 326.

We have seen, considering Moorman's 'due process' challenge above, that the Iowa apportionment method, in taxing plaintiff's in-state sales, imposes taxes on factors at least as valuable as the 'sales' criterion. These factors

were identified as Moorman's capital and labor or in terms of a three factor formula—property and payroll. And as this case on its facts clearly displays, all of Moorman's property and payroll used to produce the livestock products sold here are located in Illinois. As we found above and in terms of scenario posed in *General Motors Corporation* v. *District of Columbia*, supra, at 559-60:

> "The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves."

Since Illinois taxes apportion corporate income using the three factor apportionment method, S.H.A., Sections 120-3-304 612-(3), Moorman finds its income taxed by both Iowa and Illinois exactly as the *General Motors* Court described.

We find and hold that the single sales factor of Iowa Code Section 422.33 taxes values beyond those which may be justly allocated to intrastate Iowa activity; and application of the formula results in "gross overreaching" by this State of conduct interstate in character. We conclude Iowa Code Section 422.33 on its face violates the Commerce Clause to the United States Constitution.

Another aspect of the Commerce Clause is implicated by the Iowa taxing mechanism; the burden cast upon interstate commerce by the spectre of "multiple taxation." *J. D. Adams Mfg. Co.* v. *Storen*, 304 U.S. 307, 311-12 (1938), striking an indiscriminate and unapportioned 'privilege'

tax on gross receipts from commerce, put the rule this way:

> "The vice of the statute as applied to receipts from interstate sales is that the tax includes in its measure, without apportionment, receipts derived from activities in interstate commerce; and that the exaction is of such a character that if lawful it may in substance be laid to the fullest extent by states in which the goods are sold as well as those in which they are manufactured. Interstate commerce would thus be subjected to the risk of a double tax burden to which intrastate commerce is not exposed and which the commerce clause forbids. We have repeatedly held that such a tax is a regulation of, and a burden upon, interstate commerce prohibited by Article I, Section 8 cf the Constitution."

In recent years a pall has been laid upon the *Adams Mfg.* "risk" of multiple taxation test. The suggestion was made in *General Motors Corporation* v. *Washington*, 377 U.S. 436 (1964) that the mere 'risk' of a taxpayer's income being subjected to double taxation would have to give way to an actual showing that the income, in fact, was bearing taxation from multiple sources. The Court of Appeals of Michigan was confronted with these differing standards in *Michigan Fruit Canners, Inc.* v. *Michigan Department of Treasury*, 53 Mich. App. 1, 218 N.W.2d 385 (1974). That Court considered a Commerce Clause challenge to Michigan's single sales factor franchise tax. Regarding the *Adams* 'risk' rule the Michigan Court noted the most recent United States Supreme Court pronouncement on the subject, *Evco* v. *Jones*, 409 U.S. 91 (1972), revitalized *Adams* and in so doing paid no regard to *General Motors Corporation* v. *Washington*, supra. The Michigan Court concluded the *Adams* rule respecting the risk

of multiple taxation remained "the" rule and applied it to the facts of that case.

Our reading of *Evco* v. *Jones*, supra, compels us to agree with the Michigan Court that *Adams* is the test that must be applied here; although we note that if the Iowa single sales factor apportionment method were sustained by this opinion, both the *Adams* 'risk' test and the *General Motors Corp.* v. *Washington* 'actual taxation' tests would be met.

The facts surrounding Moorman's tax dilemma once again become crucial in demonstrating that Iowa Code Section 422.33 runs afoul of the Commerce Clause "multiple taxation" prohibition.

Looking to Moorman's tax year of 1968 it appears that the corporation's apportionable income (that amount to which the single sales factor is applied and whose product results in Iowa taxable income) for that year amounted to $7,076,510. Since Moorman's Iowa sales relative to sales everywhere were 21.8792%, Iowa taxable income in that year, by statute, should have been $1,548,284. This is the dollar figure subjected to taxation through use of the single sales factor.

The rub is that Illinois, by use of its equally balanced three factor formula, reserves the right to tax income resulting from Iowa sales because it is in Illinois that the manufacturing process respecting goods sold here occurs—in the form of Illinois property and payroll.

Moorman submits these statistics, to which defendant has stipulated, to show in a compelling manner the taxes both States impose on the same income: For 1968, Moorman's Illinois payroll was equal to 41.00% of its total payroll. For the same year, its property in Illinois amounted to 84.29% of all property it owned. Since the

sales element of the Illinois three factor apportionment formula for 1968 was 0.00% (because only Iowa sales are at issue), Illinois will apportion 41.76% ((.33 x 41.00%) + (.33 x 84.29%) + (.33 x 0.00%)) of income from Iowa sales ($1,548,284) upon which it will apply its tax rate. Upon this same 1968 income, Iowa will impose its tax rates on 100% of that amount.

Thus the percentage of Moorman's 1968 income from Iowa sales taxed by Iowa (100%) added to the percentage of the same income Illinois would tax (41.76%) yields the total percentage of income which must bear a corporate tax between these two states: 141.76%. Applying this sum to Moorman's income from Iowa sales in that year ($1,548,284) makes clear that Moorman, in effect, pays taxes on a hypothetical $2,194,847 when their real dollar income stood at the reported $1,548,284. The amount of sales income bearing the tax burden of these two states in excess of Moorman's Iowa sales income is $646,563.

It is this amount (141.76% of real income or $646,563) this Court finds to impermissibly infringe upon Commerce Clause protections. It will not do to say: "The Constitution is not a formulary." (*State of Wisconsin* v. *J. C. Penney*, 311 U.S. 435, 444 (1940)) or to say: "There is nothing in the Constitution which requires a state to adopt the best possible system of taxation." (New York v. Latrobe, 279 U.S. 421, 427 (1929)) when the outcome is as gross and disproportionate as these figures show.

It is upon our return to the teaching of *General Motors Corporation* v. *District of Columbia*, supra, that Justice Stewart's words take on added meaning and leave no doubt of their constitutional intonation: "The use of an apportionment formula based wholly on the sales factor in the context of general use of the three-factor approach will

ordinarily result in multiple taxation of corporate net income. . . ." 380 U.S. at 559.

So with this case.

In rejoinder, it is asserted the Supreme Court has on many different occasions in the past upheld the use of single factor taxing apportionment formulae. Cited are: *Underwood Typewriter Co.* v. *Chamberlain*, 254 U.S. 113 (1920); *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271 (1924); *National Leather Co.* v. *Massachusetts*, 277 U.S. 413 (1928); *Kent-Coffey Mfg. Co.* v. *Maxwell*, 204 N.C. 365, 168 S.E. 397 (1933) *aff'd* 291 U.S. 642 (1933); and *Ford Motor Co.* v. *Beauchamp*, 308 U.S. 331 (1939). But the common thread running between all cases cited, their age, limits their significance here. To that the Supreme Court made express reference in *General Motors Corporation* v. *District of Columbia*, supra. In observing that multiple taxation of corporate net income was the effect of using the single sales factor approach, the Court drew that conclusion from the fact that the context of states' corporate tax laws in 1965 was generally oriented to the three-factor formulae. Of the thirty-eight states in 1965 levying tax on corporate incomes, twenty-six states used an equally-weighted three factor approach, three others used a substantially similar three factor vehicle. Another three used the two factor sales-property formula and only four taxed income on the basis of geographically defined sales. 380 U.S. 559, fn. 9.

Today the context is even more exaggerated. Of forty-six states levying taxes on corporate income (Nevada, South Dakota, Texas and Wyoming have no corporate income tax) only one, Iowa, retains the use of the single sales factor. In this light, it cannot remain arguable that the caveat sounded by the *General Motors* Court has the impact of mere dicta.

We find and hold that Iowa Code Section 422.33, on its face, threatens the risk of multiple taxation of Moorman's income thereby unduly burdening interstate commerce in violation of Article I, Section 8, Clause 3 of the United States Constitution.

Yet another facet of the Commerce Clause impales the Iowa apportionment method following from the line of cases of *Nippert* v. *City of Richmond,* 327 U.S. 416 (1946) and *Memphis Steam Laundry Cleaner* v. *Stone,* 342 U.S. 389 (1952). These cases may be construed as stating the rule that Commerce Clause protections are violated by burdening the free flow of interstate commerce when State law or municipal ordinance discriminatorily grants to local enterprise benefits which are withheld from interstate competitors.

While Moorman's business in Iowa is subjected to the double tax of both Iowa and Illinois, a similarly situated Iowa interstate manufacturer shipping goods, for example, to Illinois would pay taxes only in Illinois; then on the one-third portion of its business activity there represented by its Illinois sales. Assuming the Iowa based manufacturer made all of its sales extra-territorially, Iowa, because of the single sales factor, would tax none of the activity (represented by sales) that were made in Illinois. The obvious commercial advantage to the Iowa based manufacturer is that it would pay no tax here and be required in a three factor jurisdiction to pay tax merely on the sales component of its business conduct there. Justice Stewart comments on this aspect of the result of single-factor apportionment, saying:

> "Conversely, in some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in three-factor jurisdictions so that only 33% of their incomes will be subject to state taxation. In any case, the sheer inconsistency of the District formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and uneconomic pattern of plant location, and so presents an added reason why this Court must give proper meaning to the relevant provisions of the District Code." 380 U.S., at 560.

It is thus clear that the Iowa Code Section 422.33 single sales factor apportionment method contravenes the Commerce Clause in ways manifest above; and we so hold.

SAVINGS CLAUSE

In view of our holding that Iowa Code Section 422.33(1)(b) is facially unconstitutional for the reasons found above, this Court has serious reservations as to whether Iowa Code Section 422.33(2), allowing the director the discretion of applying a different apportionment formula if the result of application of the single factor formula is inequitable, can operate as a "savings clause" in view of our holdings.

Assuming *arguendo* that Section 422.33(2) could so operate, we observe that of 1,969 corporate income tax returns filed by non-Iowa manufacturers between the years 1968 through 1972 inclusive, the director has allowed only one such corporate taxpayer the privilege of using the three-factor payroll-property-sales apportionment formula expressly condoned by the *General Motors Corporation* v. *District of Columbia,* supra, Court. In balance it must be stated that of the 1,969 corporate tax returns filed for those years the director did authorize use of other apportionment formulae which were neither the single sales factor nor the three factor formula for 90 corporate taxpayers.

We conclude on these facts concerning non-Iowa manufacturers, that the largely unexercised discretion granted the director to exempt a taxpayer from the reach of Iowa Code Section 422.33 cannot save the statute from its remaining unconstitutional infringements respecting corporations not granted license, and from its timely death by this opinion.

SUMMARY OF CONCLUSIONS OF LAW

In view of the factual findings made by this Court throughout this opinion, we conclude:

(1) that Iowa Code Section 422.25 authorizes the defendant to examine and determine Moorman's tax liability for its fiscal years of 1968 and 1969 notwithstanding the three year bar of this section;

(2) that Iowa Code Section 422.33(1)(b) does not violate the Equal Protection Clauses of either United States Constitution or Iowa Constitution;

(3) that Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Due Process Clauses of both the United States Constitution and Iowa Constitution; and

(4) that Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Commerce Clause, Article I, Section 8, Clause 3, of the United States Constitution because it

(a) does not fairly apportion interstate business activity to intrastate tax values;

(b) causes multiple taxation of corporate net income by more than one taxing jurisdiction; and

(c) provides local business with a direct commercial advantage not so enjoyed by interstate business.

(5) that the apportionment percentages to be applied to Moorman's net income for the tax years in controversy in this action shall be those specified in paragraph thirty-four of the stipulation.

In response to these parties' request, no decree is now provided and the Court retains jurisdiction of this matter for ninety days within which time these parties shall come to some agreement as to the amount of Moorman's tax liability. If such agreement is not reached within said period, to begin with the filing of this opinion, the Court shall be notified within five days of the expiration of said period and such further proceedings as are necessary to the decree shall at that time be scheduled.

/s/ A. M. Critelli
Judge, Fifth Judicial District of Iowa

Original filed

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Harry M. Griger, Asst. Atty. Gen. Lucas State Office Bldg., Des Moines

James L. Rogers, John R. Phillips, Russell L. Samson, 1300 R&T Bldg., Des Moines

IN THE DISTRICT COURT OF THE STATE OF IOWA
In and for Polk County

EQUITY NO. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

RULING ON JOINT MOTION TO RECONSIDER AND SUPPLEMENTAL FINDINGS

(Filed January 7, 1977)

NOW on this 7th day of January, 1977, the above-captioned matter coming on for hearing before the undersigned on the joint oral motion of the parties, the plaintiff represented by Walter R. Brown and John V. Donnelly, the defendant by Harry M. Griger, and amicus curiae, Iowa Manufacturers Association, by James L. Rogers and Russell L. Samson, the Court having heard legal arguments of counsel and after consideration of additional authorities cited to the Court is now prepared to respond to said joint motion.

On the 17th day of December, 1976, this Court filed its findings of fact and conclusions of law in this matter. Since that time these parties have had an opportunity to examine said findings and conclusions and questions have been raised as to the scope and effect of said ruling. In light of these questions the Court believes some modification of its earlier ruling is now in order.

The requests by counsel for clarification appear to fall along four rough lines of inquiry. Each of these general areas will be separately identified and addressed below.

CORRECTED FINDINGS OF FACT

As part of its findings of fact the Court observed at page 27 of its opinion ". . . that of 1,969 corporate income tax returns filed by non-Iowa manufacturers between the years 1968 through 1972 inclusive, the director has allowed only one such corporate taxpayer the privilege of using the three-factor payroll-property-sales apportionment formula expressly condoned by the *General Motors Corporation* v. *District of Columbia*, supra, Court. In balance it must be stated that of the 1,969 corporate tax returns filed for those years the director did authorize use of other apportionment formulae which were neither the single sales factor nor the three factor formula for 90 corporate taxpayers."

To adequately reflect the facts part of the stipulation, the Court hereby strikes the above quoted language beginning with "In balance . . ." to the end of that paragraph and modifies and expands said ruling by finding the following:

> Of the 1,969 corporate tax returns filed in those years, 91 taxpayers filed on the basis of some other allocation method than the single sales factor. One taxpayer, referred to above, was expressly authorized the use of a three factor formula, while 84 taxpayers were denied resort to three factor apportionment by the director; and three taxpayers made unconsented use of a three factor formula which was put beyond challenge by operation of the statute of limitations.

SCOPE OF UNCONSTITUTIONALITY

Because the Court's December 17, 1976, ruling in this matter leaves questions to these parties' minds on the exact portions of Iowa Code Section 422.33 which was in fact declared to be unconstitutional in said ruling, the Court further delineates the specific aspect of Section 422.33 found to be infirm.

While expressed in the original ruling to be Section 422.33(1)(b) which the Court found defective, the specific portion of Section 422.33(1)(b) which was at issue and found facially unconstitutional was the third full paragraph of that section reading as follows:

> Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

Thus, the balance of Section 422.33 remains unaffected, hence valid, by the December 17 ruling.

THE VALIDITY OF REMAINING PORTIONS OF SECTION 422.33 AS A VIABLE TAXING STATUTE

In light of the confined parameters of this Court's December 17, 1976 ruling the question has been presented as to whether the remainder of Section 422.33 leaves the State of Iowa with a viable corporate taxing statute.

We think the answer to be clear and certain that the unaffected remainder of Section 422.33 itself presents a workable and valid taxing power without regard to the now excised sales factor apportionment method. That conclusion is premised on the language of Section 422.33(1).

Section 422.33(1) states:

> If the trade or business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income, but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on that portion of the net income reasonably attributable to the trade or business within the state. . . .

Since Moorman will now be required to apportion their prior years' income on the basis of the percentages found in paragraph 34 of the stipulation the amount Moorman shall hereinafter apportion to the State of Iowa is identified in the above quoted portion of 422.33(1) as that which is "reasonably attributable" to the trade or business Moorman conducts within Iowa borders. No serious question remains that the standard of Section 422.33(1) defining the income thus to be apportioned as that "reasonably attributed" to Iowa presents constitutional problems. The 'reasonably attributable' apportionment method identified there and in Section 422.33(2) presents a legitimate method of allocating income even without regard to the now stricken but more specific 'sales factor' method existing merely as the legislatively constructed mechanism by which reasonable attribution was measured. The 'reasonably attributable' apportionment method remaining as vital as ever poses no problems for a standard sufficient to withstand full constitutional scrutiny. *Elk Run Telephone Company* v. *General Telephone Company*, 160 N.W.2d 311 (Iowa 1968).

Standing as it does, Iowa Code Section 422.33 leaves the defendant full power to apportion and tax plaintiff's income.

PROSPECTIVE OPERATION OF COURT'S RULING

Fully aware of the immediate and far reaching ramifications of the December 17 ruling, the Court is inclined to believe some pronouncement as to the application of the ruling should be made.

Evidence presented by the defendant in light of our earlier ruling shows compellingly the damage to state finances and efficient government that will result if this ruling is left to operate in its full retrospective breadth. We are convinced by such evidence and awakened to the serious and far reaching consequences such a looming catastrophe presents to this State.

We are not however without power to limit the damage that surely will be visited upon the public fisc. Increasingly courts have been called upon to limit the effect in the change of the construction of a statute by announcing the operation of the new rule of law as prospective only. See *Lemon* v. *Kurtzman*, 411 U.S. 192 (1973) and *Linkletter* v. *Walker*, 381 U.S. 618 (1965). And increasingly it has been recognized that prospective application of a new rule should apply as well to cases sounding of constitutional import. *Linkletter*, at 628. That view is premised on the reality that a ruling of unconstitutionality "is an operative fact and may have consequences which cannot justly be ignored. The past cannot always be erased by a new judicial declaration." *Chicot County Drainage District* v. *Baxter State Bank*, 308 U.S. 371, 374 (1940).

Iowa cases have recognized that a court may make a decision operational on a prospective basis alone. That rule announced in *State* v. *Knox*, 186 N.W.2d 641 (Iowa 1971) is not by its terms limited to cases involving criminal conduct. See also, *Linkletter* v. *Walker*, supra, at 627;

21 C.J.S. *Courts* Section 194 at 327-28 (Supp. 1976). Nor should the rules be different in a case such as this.

It has been long recognized by similar cases from other jurisdictions that the particular urgencies attending public financial well-being and the threatened fiscal embarrassment if not insolvency of public institutions created by a ruling of unconstitutionality require that the new rule of law be mediated in its rigor by a declaration of the scope of its operation. *City of Tempe* v. *Del E. Webb Corporation*, 284 P.2d 477 (Ariz. 1971); *Southern Pacific Company* v. *Cochise County*, 377 P.2d 770 (Ariz. 1963); *Oklahoma County* v. *Queen City Lodge No. 197, I.O.O.F.*, 156 P.2d 340 (Okla. 1945); 21 C.J.S. *Courts* Section 194 (b) (1940, Supp. 1976).

We believe the overriding equities presented favor the defendant's view that the Court's ruling herein be limited to operating only in a prospective manner. But we find and hold that plaintiff Moorman should have the benefit of the ruling it generated.

We therefore find and hold that the Court's ruling herein which holds the third full paragraph of Iowa Code Section 422.33(1)(b) facially unconstitutional shall be applied prospectively, with the exception that this holding shall apply to Moorman.

The benefit of this ruling shall not be granted to those corporations who have not taken or can take no timely steps to assert or protect their rights by virtue of the filing of a claim for refund, pursuant to Iowa Code Section 422.73, or protest, pursuant to Iowa Code Section 422.28. But a taxpayer who has so protected or may so protect his rights whether by appeal, judicial review, protest, or claim for refund shall be entitled to a refund of tax paid on only that amount resulting from the dif-

ference in application of the single sales factor method of apportioning that taxpayer's income and other constitutionally appropriate apportionment formulae applied with the consent of the defendant's director. Iowa Code Section 422.33(2).

/s/ A. M. Critelli
Judge, Fifth Judicial District of Iowa

Original filed

Copies to:

Walter R. Brown
John V. Donnelly
Harry M. Griger
James L. Rogers
Russell L. Samson

IN THE DISTRICT COURT OF THE STATE OF IOWA
In and for Polk County

EQUITY NO. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

JUDGMENT AND DECREE

(Filed January 7, 1977)

NOW on this 7th day of January, 1977, this matter comes before the Court for purposes of entry of a judgment and decree upon which an appeal can immediately result, and the Court, being fully advised in the premises, hereby concludes as follows:

IT IS ORDERED, ADJUDGED, AND DECREED that the Court's Findings of Fact and Conclusions of Law, dated December 17, 1976, as modified and supplemented by the Court's Supplemental Findings, dated January 7, 1977, be incorporated herein by reference as if set forth in full.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that defendant have judgment against plaintiff for $3,975 Iowa income tax plus interest of $571 computed through January 31, 1977, for a total of $4,546 and that interest continue to accrue as provided by Section 422.25, Code of Iowa, 1973, until said judgment is paid.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that costs be assessed one-half to plaintiff and one-half to defendant.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that the bond filed herein by plaintiff is hereby discharged.

/s/ A. M. Critelli
Judge, Fifth Judicial District of Iowa

IN THE DISTRICT COURT OF THE STATE OF IOWA
IN AND FOR POLK COUNTY

Equity No. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

NOTICE OF APPEAL

(Filed January 10, 1977)

TO: MOORMAN MANUFACTURING COMPANY

WALTER R. BROWN, JOHN V. DONNELLY,
1200 Register & Tribune Bldg.
Des Moines, Iowa 50309

CLARK R. RASMUSSEN, Clerk of the District Court of Iowa, In and For Polk County.

The above named defendant hereby appeals to the Supreme Court of Iowa from that portion of the Judgment and Decree entered herein on the seventh day of January, 1977, which held that the third full paragraph of Section 422.33(1)(b), Code of Iowa, was facially unconstitutional, which held that said Judgment and Decree was partially prospective and partially retroactive in application, and which rendered judgment against Plaintiff for $3,975 Iowa corporate income tax plus interest rather than the $236,890 tax plus interest sought by defendant, and defendant hereby appeals from all rulings and orders inhering therein.

You are also notified that said appeal will be heard before the Supreme Court of Iowa in the State Capitol Building in the City of Des Moines, Iowa, as provided by law and the rules of said Court.

/s/ Richard C. Turner
Richard C. Turner
Attorney General

/s/ George W. Murray
George W. Murray
Special Assistant Attorney General

/s/ Harry M. Griger
Harry M. Griger
Assistant Attorney General
Lucas State Office Building
Des Moines, Iowa 50309
Attorneys for Defendant-Appellant

IN THE DISTRICT COURT OF THE STATE OF IOWA
IN AND FOR POLK COUNTY

Equity No. CE3-1595

MOORMAN MANUFACTURING COMPANY,
Plaintiff,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant.

NOTICE OF CROSS APPEAL

(Filed January 25, 1977)

TO: G. D. BAIR, DIRECTOR OF REVENUE, RICHARD C. TURNER, Attorney General, State of Iowa, State Capitol Building, Des Moines, Iowa, 50319, GEORGE W. MURRAY, Special Assistant Attorney General, and HARRY M. GRIGER, Assistant Attorney General, Lucas State Office Building, Des Moines, Iowa 50309, CLARK R. RASMUSSEN, Clerk of the District Court of Iowa, In and For Polk County

YOU AND EACH OF YOU ARE HEREBY NOTIFIED that the Plaintiff herein, Moorman Manufacturing Company, does now Cross Appeal to the Supreme Court of Iowa from so much of the Judgment and Decree, entered herein on January 7, 1977 (and the Court's Findings of Fact and Conclusions of Law, dated December 17, 1976, as modified and supplemented by the Court's Ruling on Joint Motion To Reconsider and Supplemental Findings dated January 7, 1977, all of which were incorporated in said Judgment and Decree), which has been appealed from herein, as is adverse to it, to-wit:

1. That portion of the Judgment and Decree finding that the third full paragraph of Section 422.33(1)(b),

Code of Iowa, (the single sales factor method of apportionment) is not unconstitutional on its face as in violation of the equal protection clause of the Fourteenth Amendment to the United States Constitution and the similar clause in Article I, Section 6 of the Constitution of the State of Iowa.

2. The failure of the Court to find and hold that the application by the Defendant to Plaintiff of the third full paragraph of Section 422.33(1)(b), Code of Iowa, violates the equal protection and due process clauses of both the United States and Iowa Constitutions, the commerce clause of the United States Constitution, and Article VIII, Section 12 of the Iowa Constitution.

3. The failure of the Court to find and hold that Defendant's Order that Plaintiff apportion its net income to the State of Iowa pursuant to the single sales factor formula provided for in Section 422.33 (1)(b), Code of Iowa violates the duties and responsibilities imposed upon Defendant by paragraph 2 of Section 422.33, Code of Iowa; or is arbitrary and capricious and from any other orders or rulings adverse to Plaintiff which pertain to the method of apportioning its net income to the State of Iowa.

YOU AND EACH OF YOU ARE HEREBY FURTHER NOTIFIED that the said Cross Appeal will come on for hearing before the Supreme Court of Iowa at the State Capitol Building in the City of Des Moines, Iowa, as provided by law and the rules of the Supreme Court.

Swift Brown and Winick
By /s/ John V. Donnelly
John V. Donnelly
1200 Register and Tribune Building
Des Moines, Iowa
(515) 283-2076
Attorneys for Plaintiff

IN THE SUPREME COURT OF IOWA

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MOORMAN MANUFACTURING COMPANY,
Appellee,

v.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Appellant.

(Filed May 25, 1977)

Appeal from the Polk District Court—Anthony M. Critelli, Judge.

The Director of Revenue appeals from ruling of the trial court that the Iowa single-sales-factor formula was facially unconstitutional in violation of due process clauses of the federal and Iowa Constitutions and commerce clause of the federal constitution. Moorman cross appeals from rulings adverse to it.— Reversed on Director's appeal and affirmed on Moorman's cross appeal.

Richard C. Turner, Attorney General, George W. Murray, Special Assistant Attorney General, Harry M. Griger, Assistant Attorney General, for appellant.

Walter R. Brown and John V. Donnelly, of Swift, Brown and Winick, of Des Moines, for appellee.

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En banc.

MASON, J.

The fundamental issue on this appeal concerns the constitutionality, facially and as applied to the circumstances present herein, of certain provisions of the Iowa corporate income tax scheme. The issue stems from the district court's ruling that the Iowa single-sales-factor formula was facially unconstitutional in violation of due process clauses of the federal and Iowa Constitutions and commerce clause of the federal constitution. The Director of Revenue (Director) appeals from this adverse ruling and plaintiff cross-appeals from rulings adverse to it. The facts were stipulated in the proceedings had in the district court and show the following.

Plaintiff, Moorman Manufacturing Company (hereinafter Moorman), is an Illinois corporation which was doing business in Iowa and elsewhere. Its principal source of income during the fiscal years in question, March 31, 1968 through March 31, 1972, was derived from the manufacture and sale of some 80 different products for feeding livestock and poultry. It is what is commonly referred to as a "unitary" business, that is, its income arises from sources and activities carried on in several states.

During the years involved Moorman had five manufacturing plants located in Illinois, Texas and Nebraska. Its products were sold by more than 2500 salesmen, employees of Moorman, in more than 30 states during the years in question.

It carries on substantial activities in the state of Iowa. With a force of over 500 employees in this state Moorman engages in continuous solicitation of Iowa customers. After sales are negotiated delivery to Iowa customers is typically made from one of the six warehouses that Moorman operates in the state. These warehouses located at Stanwood, Plainfield, Goldfield, Marcus, Atlantic and Knoxville are maintained by Moorman's employees. It did no manufacturing in Iowa. The products that Moorman sells in Iowa are all manufactured in Illinois.

Iowa imposes a tax upon the net income of domestic corporations and foreign corporations doing business in the state. Section 422.33, The Code, 1975. A corporation's "net income" is based upon its "taxable income" as computed for federal tax purposes with an allowance for certain adjustments. Section 422.35. When the trade or business of a corporation is carried on entirely within the state, the corporation is subject to Iowa taxation on the entire amount of its net income. Section 422.33(1). However, when a corporation's trade or business is carried on partly within and partly without the state, it is subject to taxation only on that portion of its net income "reasonably attributable to" the trade or business within the state. Section 422.33(1).

Two computational steps are prescribed by section 422.33(1) for determining that portion of a corporation's net income which is reasonably attributable to its Iowa activities. First, certain income, the geographical source of which is easily identifiable, is allocated to the appropriate state. Section 422.33(1)(a). The second step allocates the remaining net income in one of two ways, depending upon the nature of the corporation's activities. Where, as here, the corporation's income is derived from the manufacture or sale of tangible personal property, the

portion of its net income attributable to its Iowa activities "shall be in that proportion which the gross sales made within the state bear to the total gross sales." Section 422.33(1)(b). The statute defines "gross sales of the corporation within the state" as the "gross sales from goods delivered within the state, excluding deliveries for transportation out of the state." If a taxpayer believes this apportionment formula operates so as to subject him to taxation on a greater portion of his net income than is reasonably attributable to his Iowa activities, provision is made for an application for an alternative method of allocation. Section 422.33(2).

Moorman filed its first income tax return with the state of Iowa for its fiscal year ended March 31, 1949. Pursuant to approval of the Iowa State Tax Commission, Moorman, after allocating its interest, dividends, rents and royalties (less related expenses) within and without the state of Iowa, apportioned the remainder of its net income to the state of Iowa on the ratio that its payroll, property and sales, as computed by Moorman, within the state of Iowa bore to its payroll, property and sales everywhere in the United States, as computed by Moorman, giving equal weight (.33) to its computed payroll, property and sales factors. This method was used by Moorman in each successive income tax return filed with the state of Iowa up to and including the income tax return filed for its fiscal year ended March 31, 1960.

For its fiscal years ended March 31, 1961, 1962, 1963 and 1964, Moorman determined its income from the sale of tangible personal property in this state pursuant to the single-sales-factor formula provided for in section 422.33 (1), The Code, at the direction of the Iowa State Tax Commission.

However, beginning in its fiscal year of 1965 Moorman again applied the three-factor-property-payroll-sales formula in computing its income from the sale of tangible personal property attributable to Iowa and has applied such formula in each succeeding return filed to date, including those filed for the years in issue. The State Tax Commission did not consent to this application of the three-factor formula.

Moorman appealed to the Polk District Court from an order issued by the Director relating to Moorman's corporate income tax returns for its fiscal years ending March 31, 1968, 1969, 1970, 1971 and 1972 which required Moorman to apportion to Iowa for Iowa income tax purposes for those years its net income derived from the manufacture and sale of tangible personal property by use of the single-sales-factor formula provided for in section 422.33 (1)(b), The Code.

Moorman's appeal to the district court involved an attack on the Iowa single-sales-factor formula on three basic grounds which were: (1) The Iowa single-sales-factor formula is facially unconstitutional; (2) The Iowa single-sales-factor formula is unconstitutional, as applied to Moorman's net income; and (3) The failure of the Director to allow Moorman the use of an alternative apportionment formula constituted an abuse of the Director's discretion granted him under section 422.33(2), The Code, 1975.

The three-factor formula employed by Moorman in computing its income from the sale of tangible personal property attributable to Iowa for the years 1968 through 1972 is explained by the Director in his brief and argument in this fashion: A unitary multi-state corporation computes its total net business income from all sources

according to the laws of the taxing state. The corporation then computes a payroll factor, the numerator of which is the payroll in the taxing state and the denominator of which is the total corporate payroll everywhere. The corporation then computes a property factor, the numerator of which is the value of the property in the taxing state and the denominator of which is the total corporate property value located everywhere. Property rented by the corporation from others is generally included in the property factor under special rules. The corporation then computes a sales or gross receipts factor, the numerator of which is the gross sales or receipts in the taxing state and the denominator of which is the total corporate gross sales or receipts everywhere.

In an effort to afford a better understanding of the results of the application of the single-factor formula and the three-factor approach we refer to the following discussion as set forth in the trial court's findings.

Moorman reported total gross sales from all of its operations in this country for the fiscal year 1968 of $97,719,800. Of that sum $22,102,015 represented sales in Iowa. Application of the single-factor formula results in the fraction of approximately 1/5—as a percentage, 22.6177%. This factor is multiplied against Moorman's net income with the product representing the income to which Iowa applies its rates.

The three-factor approach used by Moorman works in this manner: The Iowa sales percentage (22.6177%) is given one-third weight (.33 x 22.6177%), as are the elements of payroll and property. Moorman's Iowa property holdings for the year represent merely 1/25 of the property it owns everywhere—4.0753%. Moorman's payroll for that year amounted to $23,919,381 of which $3,739,426 was paid to its Iowa salesmen and warehousemen. A fraction between 1/6 and 1/7 of its entire year's payroll went to Iowa wage earners—15.6335%. The property factor and payroll factor are given equal weight with the sales factor so that the weighted percentage applied to Moorman's net income for that year is: (.33 x .226177) plus (.33 x 0.40753) plus (.33 x .156335) or .141088 or 14.1088%. This decimal is thus contrasted to the product gained from the single-sales-factor formula alone; here, .226177.

In ruling on Moorman's various contentions, the district court held, in pertinent part, as follows:

"In view of the factual findings made by this Court throughout this opinion, we conclude:

"(1) • • •;

"(2) That Iowa Code Section 422.33(1)(b) does not violate the Equal Protection Clauses of either United States Constitution or Iowa Constitution;

"(3) That Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Due Process Clauses of both the United States Constitution and Iowa Constitution; and

"(4) That Iowa Code Section 422.33(1)(b) is facially unconstitutional in violation of the Commerce Clause, Article I, Section 8, Clause 3, of the United States Constitution because it

"(a) does not fairly apportion interstate business activity to intrastate tax values;

"(b) causes multiple taxation of corporate net income by more than one taxing jurisdiction; and

"(c) provides local business with a direct commercial advantage not so enjoyed by interstate business.

"(5) • • •."

The following is an overview of the issues presented herein by the contentions asserted in both appeals:

1. *Facial Constitutionality—Due Process.*

The Director maintains the district court's determination that the exclusive use of the sales-factor formula for allocating the income of a multi-state corporation to the appropriate states, mandated by section 422.33(1)(b), was, on its face, violative of the due process clauses of the Iowa and federal constitutions, is erroneous as a matter of law. Specifically, the Director maintains Moorman's argument, adopted by the district court, that section 422.33(1)(b) taxes income-producing activities wholly outside the boundaries of Iowa and thus violates the constitutional principle of due process, is not supported by and is contrary to case law authority.

2. *Facial Constitutionality—Commerce Clause.*

As noted, the district court held, on three separate grounds, that section 422.33(1)(b) violated, on its face, the commerce clause of the federal constitution. The Director maintains the "test" used to determine the constitutionality of an income apportionment formula when challenged as violative of due process is the same "test" utilized when such a formula is analyzed with respect to a possible violation of the commerce clause. As a result, the Director's contention that section 422.33(1)(b) does not violate the principle enunciated in the commerce clause is buttressed by the same arguments and authorities set out in the "due process" portion of the Director's brief. Moorman, on the other hand, maintains the district court's determination is well supported by case law authority and is eminently sound.

3. *Facial Constitutionality—Equal Protection.*

The trial court concluded equal protection concepts were not violated by section 422.33(1)(b), on its face. On its cross appeal, Moorman contends the district court's determination was erroneous as a matter of law. Specifically, it is argued the exclusive use of the sales-factor formula results in a corporation being taxed on an amount of its net income which bears no relation to the corporation's activities in the state nor the benefits received by the corporation from the state. Moorman maintains section 422.33(1)(b) "blatantly discriminates" against corporations whose manufacturing facilities are outside of Iowa in light of the fact those corporations are taxed in the same manner as corporations whose manufacturing facilities are located within the state and thus enjoy the benefits afforded them by the state. The Director counters Moorman's arguments by asserting all corporations similarly situated are treated equally by the Iowa scheme. In addition, the Director claims Moorman did not sustain its burden of demonstrating that no rational basis exists for the classifications established by section 422.33(1)(b).

4. *Constitutionality, As Applied—Due Process.*

The district court concluded Iowa's sales-factor apportionment formula was facially violative of the due process clauses of the Iowa and federal constitutions and was likewise contrary to the commerce clause of the federal constitution. In light of that conclusion the trial court deemed it unnecessary to resolve Moorman's contention section 422.33(1)(b), as applied to Moorman, was contrary to principles of due process. The Director, relying upon the fact the trial court looked to the factual circumstances herein demonstrated by the parties' stipu-

lation thereto, contends the district court actually concluded section 422.33(1)(b) was violative of due process as applied to Moorman rather than on its face.

Consequently, it is urged this issue is the crux of the controversy. The Director claims section 422.33(1)(b) is not violative, as applied, of Moorman's due process rights, relying upon the alleged fact Moorman is not "unique" in conjunction with claimed case law support for the validity of this type of apportionment formula. Moorman, however, maintains the district court appropriately analyzed the facial validity of the sales-factor formula and found it wanting with respect to due process concepts. In the alternative, Moorman argues that should this court conclude section 422.33(1)(b) is facially free from constitutional defect, its application to Moorman amounts to a denial of due process, relying upon the arguments posited in the facial due process portion of its brief and argument.

5. *Constitutionality, As Applied—Commerce Clause.*

Again, in light of its ultimate conclusion, the district court did not feel it necessary to resolve Moorman's contention concerning the constitutionality of section 422.33(1)(b), as applied, with respect to the commerce clause of the federal constitution. If this court determines section 422.33(1)(b) is not facially constitutionally defective, Moorman seeks relief by way of this contention, relying upon alleged case law support and its previously referred to commerce clause argument. The Director, again arguing that commerce clause and due process considerations are substantially identical, relies upon his previously referred to commerce clause and due process arguments and maintains no constitutional violation is present under these circumstances.

6. *Constitutionality, As Applied—Equal Protection.*

This issue was not resolved by the district court for the previously referred to reason. Moorman contends application of section 422.33(1)(b) to it results in a denial of equal protection, citing as support therefor the equal protection argument asserted in its challenge to the facial validity of the subject statute. The Director seeks to rebut those contentions by pointing to department of revenue statistics which demonstrate Moorman was not treated differently from other similarly situated taxpayers. In addition, the Director again points to alleged case law support for the proposition that no specific income apportionment formula is constitutionally required.

7. *Constitutionality, As Applied—Article VIII, Section 12, Iowa Constitution.*

Moorman, on cross appeal, points to department of revenue records demonstrating that one foreign manufacturing corporation was permitted by the Director to apportion its net income according to a formula other than that prescribed by section 422.33(1)(b) and argues such fact constitutes a violation of Article VIII, section 12, of the Iowa Constitution, which prohibits such "exclusive privileges." The Director contends that constitutional provision has no application to administrative as opposed to legislative acts, or, in the alternative, cannot serve as the basis for Moorman's requested relief in the absence of a demonstration of discriminatory taxation with respect to similarly situated corporations. No mention of this issue can be found in the district court's ruling.

8. *In ordering Moorman to comply with section 422.33(1)(b), did the Director contravene the duties and responsibilities imposed upon him by section 422.33 and act arbitrarily and capriciously?*

Moorman contends the Director's denial of Moorman's request for an alternative apportionment formula, pursuant to section 422.33(2), violated the duties imposed upon the Director by said section in light of the fact it was clearly demonstrated the sales-factor formula did not result in the allocation to Iowa of that portion of Moorman's net income which was reasonably attributable to Moorman's Iowa business activities. Moorman argues such refusal was the result of a "total abdication of duty" and was arbitrary and capricious. The Director maintains an alternative formula is only available to a taxpayer if the application of the sales-factor approach results in the very constitutional deficiencies which are allegedly involved herein. In other words, it is the Director's position this issue is meaningless in light of the fact any resolution of the constitutional issues involved herein disposes of Moorman's contention. Consequently, the Director again advances his previous constitutional arguments. This issue was not confronted by the trial court.

9. *Retroactivity or prospectivity of a determination section 422.33(1)(b) suffers constitutional deficiencies.*

Resolution of this issue is complicated by a vague record with respect to procedural aspects connected therewith. At this point, suffice it to say Moorman contends this issue is not before this court since it was not raised below. In the alternative, Moorman argues the scope of any decision herein is controlled by section 422.73, which establishes limitations upon the timeliness of refund requests. The Director, on the other hand, argues this court

must define the scope of any determination invalidating section 422.33(1)(b) and posits guidelines in this regard. The district court held its ruling would apply to Moorman and all similarly situated corporations not foreclosed by the time limitations established by sections 422.28 and 422.73.

I. At the outset, this court employs several well settled principles in dealing with questions of a statute's constitutionality:

It is well settled, with notable exceptions not here involved, that all presumptions are in favor of the constitutionality of a regularly enacted statute.

Where the constitutionality of a statute is merely doubtful, this court will not interfere, as it must be shown that legislative enactments clearly, palpably and without doubt infringe upon constitutional rights before an attack will be upheld.

Moorman, as the attacking party, has the burden to demonstrate beyond a reasonable doubt the act violates the constitutional provisions invoked and to point out with particularity the details of the alleged invalidity. To sustain this burden it must negative every reasonable basis which may support the statute. State v. Kueny, 215 N.W.2d 215, 216-217 (Iowa 1974); Sampson v. City of Cedar Falls, 231 N.W.2d 609, 612 (Iowa 1975); State v. Kramer, 231 N.W.2d 874, 879-880 (Iowa 1975); State v. Aldrich, 231 N.W.2d 890, 894 (Iowa 1975); Avery v. Peterson, 243 N.W.2d 630, 633 (Iowa 1976); City of Waterloo v. Selden, ... N.W.2d ....., ... (Iowa 1977).

Keasling v. Thompson, 217 N.W.2d 687, 690 (Iowa 1974), states this principle:

"The judicial branch of the government has no power to determine whether legislative Acts are wise or unwise, nor has it the power to declare an Act void unless it is plainly and without doubt repugnant to some provision of the Constitution. * * * [citing authority]."

In the field of taxation, it would appear the above principles somewhat understate the deference accorded the legislature. In this regard, see 71 Am.Jur.2d, State and Local Taxation, section 96, page 417 and 84 C.J.S., Taxation, section 7, pages 53-54.

In Butler Brothers v. McColgan, 315 U.S. 501, 507, 62 S.Ct. 701, 704, 86 L.Ed. 991, 996, citing authorities, the Court declared that one who attacks a formula of apportionment of income of a corporation doing business in several states carries the distinct burden of showing by "clear and cogent evidence" that it results in extraterritorial values being taxed by the taxing state.

II. As stated, the trial court held the apportionment provision of the Iowa corporate income tax was facially unconstitutional, in violation of due process clauses of the federal and Iowa Constitutions and commerce clause of the federal constitution.

When a corporation's trade or business is carried on partly within and partly without the state, its tax base generally cannot satisfactorily be identified or segregated on a geographical basis. Due to the impracticability of so identifying or segregating the tax base of such a unitary business resort is made to apportionment formulae as a rough means of attributing a reasonable share of the tax base to the taxing state. These considerations are especially pertinent to the taxation of net income, which is at issue here. The net income or profits of a business frequently are "earned by a series of transactions beginning

with manufacture in [one state] and ending with sales in other states," and "[t]he Legislature, in attempting to put upon this business its share of the burden of taxation, [is] faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders." Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 120-121, 41 S.Ct. 45, 46-47, 65 L.Ed. 165, 169.

In regard to the two previously mentioned computational steps prescribed by section 422.33(1) for ascertaining the Iowa portion of the corporation's net income we point out that the initial step is to assign to Iowa the interest, dividends, rents and royalties received in connection with the business inside Iowa and to assign to non-Iowa sources such income received in connection with business outside the state. All income thus assigned is deducted from the overall federally-based determination of net income that would have been taxable by Iowa if the corporation in question had carried on its entire business within the state.

The income which remains after the first step in the statutory procedure is dealt with in one of two ways. In some cases, which are not of concern here, the remaining income may be specifically allocated within and without the state pursuant to rules and regulations promulgated by the director. In other cases the legislature, recognizing the difficulty of specifically allocating to various jurisdictions the net income remaining after assignment of interest, dividends, etc., provided for apportionment of such income to various jurisdictions by an apportionment formula. Accordingly, when corporations are engaged in the manufacture or sale of tangible personal property partly within and partly without the state where there is ordinarily no satisfactory means of determining the pre-

cise jurisdictional source of net income derived for that activity, the statute provides:

"Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales." Section 422.33(1)(b), The Code.

An apportionment formula, whether a single factor, two factor, or three factor, must be applied against a computed net income. The "net income" of a corporation is defined in section 422.35 to include taxable income properly computed for federal income tax purposes under the Internal Revenue Code of 1954 with certain adjustments, one of which is an equitable deduction for 50 percent of federal income taxes paid during the tax or income year.

The Supreme Court has recognized that such formulae, which owe their very existence to the absence of exact alternatives for dividing the tax base of a unitary business, cannot be expected to achieve precision.

"* * * [T]his Court has long realized the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities * * * and has declared that 'rough approximation rather than precision' is sufficient. Illinois Central Ry. v. State of Minnesota, 309 U.S. 157, 161, 60 S.Ct. 419, 422, 84 L.Ed. 670." International Harvester v. Evatt, 329 U.S. 416, 422, 67 S.Ct. 444, 447, 91 L.Ed. 390, 395.

In Nashville, C. & St. L. Ry. v. Browning, 310 U.S. 362, 365-366, 60 S.Ct. 968, 970, 84 L.Ed. 1254, 1256, "* * * the problem to be solved * * * [was] what portion of an interstate organism may appropriately be attributed to each of the various states in which it functions. Basic to the accommodation of these conflicting state and national in-

terests is realization that by its very nature the problem is incapable of precise and arithmetical solution. * * *

"* * * In a matter where exactness is concededly unobtainable and the feel of judgment so important a factor, we must be on guard lest unwittingly we displace the tax officials' judgment with our own."

Hence, it is not necessary that a state demonstrate its use of the single-factor formula has resulted in an exact measure of value. However, when a taxpayer comes forward with strong evidence tending to prove the formula employed will yield a grossly distorted result in its particular case, the state is obliged to counter that evidence to make the accommodation necessary to assure that its taxing power is confined to its constitutional limits. Norfolk & W. Ry. Co. v. Missouri State Tax Com'n, 390 U.S. 317, 329, 88 S.Ct. 995, 1003, 19 L.Ed.2d 1201, 1210.

In Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell, 283 U.S. 123, 135, 51 S.Ct. 385, ..., 75 L.Ed. 879, 908, the Court upset the application of a state apportionment formula upon a showing by the taxpayer that the percentage of income attributable to the taxing state was in fact "out of all appropriate proportion to the business transacted" by the taxpayer in the taxing state.

It appears to be well settled that a corporation doing business in several states challenging a formula of apportionment of income has the heavy burden of proving by "clear and cogent evidence" that the apportionment is grossly and flagrantly excessive. In support, see Norfolk & W. Ry. Co. v. State of North Carolina, 297 U.S. 682, 688, 56 S.Ct. 625, 628, 80 L.Ed. 977, 982.

Although, as stated, the trial court's ruling the Iowa single-sales-factor formula was facially unconstitutional in violation of due process is based upon the provisions

of both the federal and Iowa Constitutions, a separate discussion of the two constitutional provisions is not necessary under the general principle that similar constitutional guarantees are usually deemed to be identical in scope, import and purpose. Davenport Water Co. v. Iowa State Commerce Com'n, 190 N.W.2d 583, 593 (Iowa 1971).

Initially, the Director's contention the district court actually concluded section 422.33(1)(b) was violative of due process as applied, rather than on its face, can be disposed of summarily. It is true, as the Director contends, that in reaching its determination the district court refered to the stipulated factual circumstances present herein. However, reference to those facts was for the purpose of explaining the general operation of the statute in order to assess its facial validity. The Director's claim the trial court's analysis was inconsistent with its conclusion is without merit.

In reaching the conclusion section 422.33(1)(b), on its face, contravened principles of due process, the district court made the following analysis:

"In subjecting Moorman's arguments to due process scrutiny the initial inquiry must be whether 'the taxing power exerted by the state bears a relation to protection, opportunities and benefits given by the state. The simple, but controlling question is whether the state has given anything for which it can ask return.' State of Wisconsin v. J. C. Penney Co., 311 U.S. 435, 444 (1940) [61 S.Ct. 246, 250, 85 L.Ed. 267, 270-271, 130 A.L.R. 1229, 1233]. * * *

"Of course, Moorman, first and foremost, is accorded the not invaluable right to do business in the State of Iowa. The record shows its sales in Iowa are substantial. It is given the protection of Iowa laws with resort to the Iowa court system * * *. It is certain that Moorman's business

presence and activities in Iowa with this State's consent constitute the 'minimum connection' by which Iowa can constitutionally levy a corporate tax.

"The more narrow question presented, however, acknowledging that '. . . the tax * * * has relation to opportunities, benefits (and) protection conferred or afforded by (Iowa is whether) the tax is fairly apportioned to the commerce carried on within (this State). Norfolk & Western Railway Co. v. Missouri State Tax Commission, 390 U.S. 317, 325 (1968) (fn 5) [88 S.Ct. 995, 1001, 19 L.Ed.2d 1201].

"Said further by the *Norfolk & Western Railway* Court, * * * '* * * The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due. A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to "project the taxing power of the state plainly beyond its borders." (cited cases) Any formula used must bear a rational relationship, both on its face and in its application, to property values connected with the taxing State.'

"* * *

"While accepting the right of Iowa to tax its corporate income for the services, this State renders, it [Moorman] maintains that Iowa cannot tax *all* of Moorman's income, because only a small proportion of servicing inputs arise from its relation with this State. Since the largest quantum of capital and labor respecting its product sold here results from its Illinois relationship, the Iowa apportionment formula fails to reasonably apportion profits traceable to Illinois operations and taxes those

activities occurring in Illinois. In this sense, says Moorman, the single sales factor taxes more than that which should be fairly apportioned to Iowa and, as a consequence, violates its constitutional rights of due process * * *.

"We agree."

In support of its conclusion the district court relied heavily upon statements of the Court in General Motors Corp v. District of Columbia, 380 U.S. 553, 85 S.Ct. 1156, 14 L.Ed.2d 68.

In support of the trial court's ruling Moorman contends the Iowa single-sales-factor formula is facially unconstitutional in violation of due process of law because the formula attempts to tax *all* of the profits arising from sales of tangible personal property in Iowa even though the product is manufactured outside this state; thus, the single-sales-factor formula takes no cognizance of the contribution which the creation of the product outside the state makes to the realization of profit.

Moorman also asserts the Iowa single-sales-factor formula is facially unconstitutional in violation of the commerce clause of the United States Constitution because the formula does not fairly apportion net income to Iowa, causes multiple taxation of corporate net income by two or more states, and provides Iowa corporate businesses with direct commercial advantage not enjoyed by non-Iowa interstate business.

The sum of Moorman's argument is that the Iowa single-sales-factor formula is without economic or legal justification.

The Director, on the other hand, insists the formula provided in section 422.33(1) imposes a tax only on the

portion of net income reasonably attributable to the trade or business within Iowa.

At this point, it should be noted the Director's contention the same "test" is applicable with respect to both a constitutional challenge to the apportionment formula established by section 422.33(1)(b), based upon due process and a similar challenge founded upon the provisions of the commerce clause has some merit. However, while similar considerations are involved in the two constitutional determinations, it would be an overstatement to say they are identical. Notwithstanding some overlap, they will be dealt with separately herein. See Standard Pressed Steel Co. v. Washington Dept. of Rev., 419 U.S. 560, 95 S.Ct. 706, 42 L.Ed.2d 719.

In support of the contention the district court erroneously concluded section 422.33(1)(b) facially contravened due process guarantees, the Director asserts that the United States Supreme Court has never so held, and in fact, has consistently upheld single-factor apportionment formulae. He maintains the taxpayers in those cases which upheld single-factor formulae posited constitutional arguments identical to those asserted by Moorman to no avail, notwithstanding the fact that the tax schemes involved therein were much more harsh than Iowa's corporate tax scheme. Consequently, the Director maintains Moorman's allegations and the district court's determination are untenable.

In State of Wisconsin v. J. C. Penney Co., supra, 311 U.S. at 444, 61 S.Ct. at 249-250, 85 L.Ed. at ....., 130 A.L.R. at 1232-1233, is the following:

"The Constitution is not a formulary. It does not demand of states strict observance of rigid categories nor precision of technical phrasing in their exercise of the most

basic power of government, that of taxation. For constitutional purposes the decisive issue turns on the operating incidence of a challenged tax. A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society."

The Director relies heavily upon the sentiments expressed in the above opinion and upon a number of cases of the Supreme Court which approve single-factor apportionment formulae. See Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 41 S.Ct. 45, 65 L.Ed. 165; Bass, Ratcliff & Gretton v. State Tax Commission, 266 U.S. 271, 45 S.Ct. 82, 69 L.Ed. 282; National Leather Co. v. Massachusetts, 277 U.S. 413, 48 S.Ct. 534, 72 L.Ed. 935; Ford Motor Co. v. Beauchamp, 308 U.S. 331, 60 S.Ct. 273, 84 L.Ed. 304; Kent-Coffey Manufacturing Company v. Maxwell, 204 N.C. 365, 168 S.E. 397, 90 A.L.R. 476, aff'd., 291 U.S. 642, 54 S.Ct. 437, 78 L.Ed. 1040. It cannot be denied these cases are in fact supportive of the Director's contentions.

The Court has emphasized two points in evaluating the contention under the due process clause that an apportionment formula attributes more property or income to a taxing state than it may rightly claim. First, the Court has recognized that the very nature of the undertaking—the resort to a mathematical formula to determine the state's share of a business entity's tax base where there is no satisfactory way of determining it directly—involves rough approximation; and the Court has repeatedly held that the due process clause requires nothing more exacting. Second, the Court has made it plain that a taxpayer challenging an apportionment formula has more than the usual

heavy burden of proving by clear and convincing evidence that the application to it of the formula produces a grossly disproportionate result. Another basic principle which has emerged from the opinions of the Supreme Court recognizes that states are given the utmost leeway both in their choice and application of formulae for apportioning the net income of a corporation whose trade or business is carried on partly within and partly without its borders as long as basic considerations of due process and equal protection are observed.

The foregoing statements constitute a fair summary of the decisions of the Court in the cited cases.

With these principles in mind it is argued that in order to sustain the trial court's holding the apportionment formula prescribed in section 422.33(1) is "facially unconstitutional" this court would be required to conclude such a formula by its very terms will necessarily produce a "grossly distorted result" or an apportionment "out of all proportion to the business transacted."

We examine this contention in light of General Motors Corp. v. District of Columbia, 380 U.S. 553, 85 S.Ct. 1156, 14 L.Ed.2d 68, which was relied upon by the trial court in reaching its conclusion and by Moorman in its effort to support the trial court's ruling.

In the cited case the Court was faced with constitutional and statutory challenges to the method of apportionment utilized to determine tax liability under a franchise tax exacted by the District of Columbia. The statute in question provided for taxation on that portion of a corporation's net income which was "fairly attributable" to its activities within the District and authorized the tax commissioner to prescribe regulations concerning the appropriate apportionment formula to be used. General Motors

challenged the sales-factor formula on the ground it attributed to the District an unreasonably high proportion of its total income, and consequently, was contrary to the provisions of the enabling statute and violative of the due process and commerce clauses of the federal constitution.

The Court determined the sales-factor formula was contrary to the statute which authorized the collection of said tax and thus reversed the lower court "without reaching the constitutional questions raised." 380 U.S. at 555, 85 S.Ct. at 1158, 14 L.Ed.2d at .....

We quote from the opinion:

"The conclusion which we reach by analysis of the plain language of the statute also finds support in the consequences which a contrary view would have for the overall pattern of taxation of income derived from interstate commerce. The great majority of States imposing corporate income taxes apportion the total income of a corporation by application of a three-factor formula which gives equal weight to the geographical distribution of plant, payroll, and sales. The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves. Conversely, in some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in the three-factor jurisdictions so that only 33% of their incomes will be subject to state taxation. * * *

"Moreover, the result reached in this case is consistent with the concern which the Court has shown that state taxes imposed on income from interstate commerce be fairly apportioned. In upholding taxes imposed on corporate income by Connecticut and New York and apportioned in accordance with the geographical distribution of a corporation's property, this Court carefully inquired into the reasonableness of the apportionment formulae used.

" 'The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut and ending with sale in other states. In this it was typical of a large part of the manufacturing business conducted in the state. The Legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. * * * There is * * * nothing in this record to show that the method of apportionment adopted by the state was inherently arbitrary, or that its application to this corporation produced an unreasonable result.' Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 120-121, 41 S.Ct. 45, 47, 65 L.Ed. 165. See also Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n, * * * [supra]. While the Court has refrained from attempting to define any single appropriate method of apportionment, it has sought to ensure that the methods used display a modicum of reasonable relation to corporate activities within the State. The Court has approved formulae based on the geographical distribution of corporate property and those based on the standard three-factor formula. * * * [citing authorities]. The standard three-factor formula can be justified as a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates. By contrast, the geogra-

phical distribution of a corporation's sales is, by itself, of dubious significance in indicating the locus of either factor. We of course do not mean to take any position on the constitutionality of a state income tax based on the sales factor alone. For the present purpose, it is sufficient to note that the factors alluded to by this Court in justifying apportionment measures constitutionally challenged in the past lend little support to the use of an exclusively sales oriented approach. In construing the District Code to prohibit the use of a sales-factor formula, we sacrifice none of the values which our scrutiny of state apportionment measures has sought to protect." 380 U.S. at 559-561, 85 S.Ct. at 1160-1161, 14 L.Ed.2d at .....

Although the Court in *General Motors* by way of dictum criticized the single-sales-factor apportionment formula it "refrained from attempting to define any single appropriate method of apportionment," and explicitly pointed out that its decision was not based on constitutional grounds when it said, "We of course do not mean to take any position on the constitutionality of a state's income tax based on the sales factor alone."

We have recognized the principle that courts have a duty to avoid constitutional questions when merits of a case may be fairly decided without facing such questions.

In Collier v. Denato, 247 N.W.2d 236, 241 (Iowa 1976), we quoted with approval this statement from State v. Thomas, 219 N.W.2d 3, 4 (Iowa 1974):

"• • • We prefer to decide cases on nonconstitutional grounds when possible. City of Des Moines v. Lohner, 168 N.W.2d 779, 782 (Iowa) ('We do not consider constitutional questions unless it is necessary for the disposition of the case.'); 16 Am.Jur.2d Constitutional Law § 113 at 301; 16 C.J.S. Constitutional Law § 94 at 317 ('The principle that

necessity of determination is a condition to judicial consideration of constitutional questions also finds application in the rule that such questons will not be passed on where the issues involved in the particular case may be decided on another ground, even though the constitutional issue has been properly presented.') • • •."

The same principle is announced in Alma Motor Co. v. Timken-Detroit Axle Co., 329 U.S. 129, 136, 67 S.Ct. 231, 234, 91 L.Ed. 128, 133 and authorities cited in footnote 8. See also Kovacs v. Brewer, 356 U.S. 604, 607, 78 S.Ct. 963, 966, 2 L.Ed.2d 1008, ...

Nevertheless, where the Court has employed the principle of avoidance of constitutional issues language used in such a decision does not afford a satisfactory basis for determining a state statute unconstitutional on its face. This is particularly true in light of the well-settled principles set out in division I hereof which this court adheres to in dealing with questions of a statute's constitutionality.

As noted, the burden is on the attacking taxpayer to demonstrate beyond a reasonable doubt that the act challenged here is unconstitutional on its face. There is nothing inconsistent with this principle and that announced in Butler Brothers v. McColgan, 315 U.S. at 507, 62 S.Ct. at 704, 86 L.Ed. at 996, that one who attacks a formula of apportionment of income of a corporation doing business in several states carries the distinct burden of showing by "clear and cogent evidence" that it results in extra-territorial values being taxed by the taxing state. The phrase "beyond a reasonable doubt" refers to the quantum of evidence necessary to sustain the attacking party's challenge on constitutional grounds, whereas the phrase "clear and cogent evidence" refers to the quality of evidence which must be offered by such party in an effort to sustain his burden of proof as to application of the formula issue.

There is another reason why we feel the *General Motors* decision is not determinative of the question considered in this division. As counsel points out, the statutory language on which decision turned in *General Motors* was not the provision making "net income * * * as is fairly attributable" to the District taxable; rather it was the specific requirement that net income derived from a trade or business carried on within and without the District shall "be deemed to be income from sources within and without the District." It was the Court's interpretation of this statutory phrase—which has no analogue in the Iowa statute and can scarcely be found in the due process clause—which was the fulcrum of the Court decision.

A search of the citator discloses General Motors Corp. v. District of Columbia has been cited in State Loan and Finance Corp. v. District of Columbia, 381 F.2d 895, 902 (D.C. Cir. 1967), on a proposition not involved here. We are unaware of any decision, federal or state, where it has been cited on the issue before us.

As noted, in its opinions in this area the Supreme Court has recognized: (1) the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as the unitary business under consideration here; (2) rough approximation rather than mathematical precision is sufficient; (3) the heavy burden cast upon the taxpayer in challenging a legislative enactment on constitutional grounds; and (4) the utmost leeway must be given the states both in their choice and application of formulae in this connection as long as basic considerations of due process and equal protection are observed.

In light of those principles we conclude section 422.33(1) calls for a method of allocation which is fairly calculated to assign to Iowa only that portion of the tax-

payer's net income reasonably attributable to the trade or business done in Iowa since the taxing power exerted by this statute bears fiscal relation to the protection, opportunities and benefits given by the state. See Complete Auto Transit, Inc. v. Brady, ____ U.S. ____, 97 S.Ct. 1076, 1083, ____ L.Ed.2d ____. It is settled law that a state which provides an orderly market in which to transact business confers benefits which constitutionally justify the levy of an income tax. State of Wisconsin v. J. C. Penney Co., 311 U.S. 435, 61 S.Ct. 246, 85 L.Ed. 267.

It cannot logically be maintained that the apportionment formula prescribed by section 422.33(1) with the adjustments provided for in section 422.35 will necessarily produce a "grossly distorted result" or an apportionment "out of all proportion to the business transacted" in every conceivable situation which might possibly arise.

Thus far we have referred to only one of the fiscal years in issue—1968—in stating the percentage produced by application of the single-factor formula—22.617. The summary of exhibits 15 and 16 in Moorman's brief and argument shows application of this formula produced a percentage of 21.21 for 1969, 19.95 for 1970, 18.95 for 1971, and 18.67 for 1972.

Moorman points out employment of the three-factor formula would have resulted in a lower percentage for use in computing its income from sale of tangible personal property attributable to Iowa in those years.

However, the mere fact application of the single-factor formula results in a larger percentage being used for ascertaining the Iowa portion of the corporation's net income than would application of some other type of formula does not render the apportionment provision of the Iowa corporate income tax law facially unconstitutional

in violation of due process clauses of the federal and state constitutions. Such evidence alone does not establish that the difference between the two figures represents either double taxation or a taxation of extraterritorial values. Fairness is not equated with absolute precision.

In our opinion the formula in question meets the due process requirement of attempting to fairly allocate the corporation's income. In support of this conclusion see General Motors Corporation v. State, 181 Colo. at ....., 509 P.2d at 1266, and authorities cited.

The statute is free from the constitutional infirmities asserted and considered in this division. The trial court erred in holding otherwise.

III. The district court determined section 422.33(1)(b), on its face, contravened the principles embodied in the commerce clause of the federal constitution. The Director maintains such determination is erroneous as a matter of law.

The Director, perhaps overstating the similarity between the two constitutional analyses, does not distinguish between his due process and commerce clause contentions. The authorities and arguments posited in support of the former are likewise offered as supportive of the latter.

The considerations applicable to the resolution of a due process challenge to an apportionment formula are substantially similar to those utilized in assessing the validity of that formula with respect to the commerce clause. Extraterritorial taxation is constitutionally defective "both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due." Norfolk & W. Ry. Co. v. Missouri State Tax Com'n, supra, 390 U.S. at 325, 88 S.Ct. at 1001, 19 L. Ed.2d at .....

The commerce clause prohibits a state from exacting a tax from an interstate corporation which is determined through application of inappropriate apportionment formulae, and consequently, subjects interstate commerce to the risk of multiple taxation. J. D. Adams Mfg. Co. v. Storen, 304 U.S. 307, 311-312, 58 S.Ct. 913, 916, 82 L.Ed. 1365; Gwin, White & Prince v. Henneford, 305 U.S. 434, 438-440, 59 S.Ct. 325, 327-328, 83 L.Ed. 272; Central Railroad Co. v. Commonwealth of Pa., 370 U.S. 607, 612, 82 S.Ct. 1297, 1301, 8 L.Ed.2d 720; Standard Pressed Steel Co. v. Washington Dept. of Rev., supra, 419 U.S. at 563-564, 95 S.Ct. at 709, 42 L.Ed.2d at ..... As a result of said multiple taxation, interstate commerce is put at a commercial disadvantage with respect to its local counterpart.

Moorman, relying upon the first paragraph of that portion of the General Motors Corp. v. District of Columbia opinion set out in division II, contends the apportionment formula prescribed by section 422.33(1)(b) results in multiple taxation of interstate commerce and a consequent, illegitimate benefit to Iowa manufacturers. Specifically, it maintains the sales-factor apportionment formula, on its face, subjects corporations manufacturing goods outside of Iowa and selling goods within this state to a tax on all income from their Iowa sales while the manufacturing states are also entitled to tax a portion of such income. In other words, Moorman assails the facial validity of 422.33(1)(b) on the ground it results in the taxation of more than 100% of a corporation's income from its Iowa sales. In addition, Moorman points out Iowa manufacturing corporations are not subject to such multiple taxation, and consequently, are the recipients of a statutorily based illegitimate commercial advantage.

Much of the analysis advanced in the previous division is of assistance in the resolution of Moorman's com-

merce clause contentions. Again, Moorman must satisfy the heavy burden of demonstrating that section 422.33(1)(b) violates the constitutional precept invoked. Furthermore, the weighty presumption of constitutionality is again operative.

Moorman's contention a foreign manufacturing corporation selling its products in Iowa is subject to tax on 100% of its income from Iowa sales ignores the provisions and application of section 422.35. That statutory provision provides for the adjustments necessary to arrive at a corporation's net income for Iowa tax purposes. A number of potentially large deductions are provided for therein, including the previously mentioned deduction of 50% of the federal tax liability incurred. Clearly, a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales. Consequently, Moorman has not demonstrated that the provisions of section 422.33(1)(b) result in a foreign corporation being taxed on more than 100% of its income from Iowa sales.

We rely again on the principles recognized by the Supreme Court in its opinions in this area as summarized in division II in concluding use of the single-sales-factor formula provided by the statute does not violate the commerce clause of the United States Constitution. The trial court erred in holding otherwise.

IV. On its cross appeal, Moorman maintains the district court erred as a matter of law in concluding section 422.33(1)(b), on its face, did not violate the guarantees of equal protection provided in the federal and state constitutions.

The district court ruled as follows with respect to Moorman's equal protection contentions:

"It is readily apparent that the statute in question focuses on the classification of 'corporations.' Since classifying corporations for different tax treatment than individual persons has most recently been sustained in Lehnhausen v. Lake Shore Auto Parts Co., 410 U.S. 356 (1973) [93 S.Ct. 1001, 35 L.Ed.2d 351], the Iowa scheme taxing corporations cannot be challenged merely because corporations are taxed. Nor does the fact that Section 422.33 establishes a graduated tax on corporate incomes lead to a finding of an invidious classification, for all corporations, without regard to any other factors, have been taxed by the same apportionment mechanism—the single sales factor. * * * [citing authority]. The simple matter is that for purposes of classification, the legislature has singled out the income for all 'corporations' as the basis on which the single sales factor is to apply; and while application of the formula yields differing amounts of tax due, for equal protection analysis, all corporations are similarly situated and are accorded exactly the same tax statement.

"This Court concludes that Iowa Code Section 422.33 on its face creates no classifications which may be found to violate Moorman's rights to equal protection of the law * * *. Indeed, Moorman's complaints concerning the operation of Section 422.33 would seem to be complaints shared by all corporations taxed by the statute whose operations are multi-state * * *."

Although Moorman argues section 422.33(1)(b) is facially invalid, its brief on cross appeal contains the following:

*"On its face, it would appear * * * section 422.33(1) does operate uniformly* upon all corporations engaged in the manufacture or sale of tangible personal property in the State of Iowa * * *.

"In fact, however, it is readily apparent that *the statute does not have a uniform operation.* * * *." (Emphasis deleted and supplied).

The quoted statements from Moorman's brief and the tenor of its contentions clearly demonstrate Moorman is in fact challenging the *application* of section 422.33(1)(b) to the particular circumstances herein. The authorities cited and arguments asserted will therefore be considered when Moorman's equal protection challenge to the sales-factor formula as applied to Moorman is considered in the next division.

In any event, even if Moorman is in fact attempting to challenge the facial validity of section 422.33(1)(b) with respect to equal protection guarantees, the contention is without merit. See City of New Orleans v. Dukes, ... U.S. ....., ..., 96 S.Ct. 2513, 2518, ... L.Ed.2d ....., ...

In Dickinson v. Porter, 240 Iowa 393, 400-401, 35 N.W. 2d 66, 72, are the following pertinent comments:

"If there is any reasonable ground for the classifications in this law and it operates equally upon all within the same class, there is uniformity in the constitutional sense and no violation of any constitutional provision invoked by plaintiff. * * * [citing authorities].

"The statute amounts to a legislative finding there are sufficient differences between property to which the act applies and other property to justify the classification. We will not interfere unless plaintiff has proven the classification does not rest on a reasonable basis but is essentially arbitrary and palpably discriminating. * * * [citing authority].

"It is well recognized the legislature has a wide discretion in determining classifications to which its acts shall

apply. * * * [citing authority]. In tax matters even more than in other fields, legislatures possess the greatest freedom in classification. * * * [citing authorities].

"It is not sufficient that the court may regard the reason for the classification a poor one. * * * [citing authorities]. The differences upon which the classification is based need not be great or conspicuous. * * * [citing authorities].

" 'An iron rule of equal taxation' is neither attainable nor necessary. * * * [citing authorities]."

Moorman's only attempt to demonstrate the unreasonableness of the classification contained in section 422.33 (1)(b) is with reference to admittedly "extreme" hypothetical situations. Such a tactic clearly does not establish the classification is unreasonable. To the extent Moorman's position is that its situation comes within one of the hypotheticals posited, the contention more appropriately deals with the validity of the statute as applied and will be considered hereinafter.

Moorman's contention section 422.33(1)(b), on its face, violates equal protection guarantees is without merit.

V. As pointed out, in view of its ultimate conclusion, the district court did not feel compelled to resolve issues presented by Moorman's contentions other than those concerning the facial constitutionality of section 422.33(1)(b).

However, since this court has determined that the single-sales-factor formula is not facially defective, Moorman's contention section 422.33(1)(b) is constitutionally deficient as applied to Moorman with respect to the due process, equal protection and commerce clauses must be dealt with.

Moorman maintains the constitutional arguments advanced for invalidating that portion of the statute on its face are equally pertinent to its claim for overturning on constitutional grounds the application of the Iowa single-sales-factor formula to its net income. Hence, it reasserts by reference the arguments previously posited in support of the facial attacks on this statute, relying again most heavily upon General Motors Corp. v. District of Columbia, supra.

This court has determined section 422.33(1)(b), on its face, is free from constitutional defect. From that determination it follows said statutory provision may generally be applied to corporate entities subject thereto without constitutional transgression. However, a statute may be constitutional with respect to some factual situations but constitutionally infirm with respect to others. Williams v. Illinois, 399 U.S. 235, 242, 90 S.Ct. 2018, 2023, 26 L.Ed.2d 586; Walker v. Johnson County, 209 N.W.2d 137, 140 (Iowa 1973); A. B. C. Distrib. Co., Inc. v. City & Cty. of San Francisco, 15 Cal.3d 566, 125 Cal. Rptr. 465, 542 P.2d 625, 628-629; 16 Am.Jur.2d, Constitutional Law, section 194; 16 C.J.S., Constitutional Law, section 71, pages 217-218.

At this point the following statement from State v. Richardson, 285 A.2d 842, 846 (Me. 1972), is apposite:

"* * * One who seeks to assert a particular conglomerate of circumstances in which the operation of the statute might be unconstitutional must prove such facts in an actual case to test the constitutionality of the statute, as applied, rather than to seek to invalidate it on its face by hypothesizing marginal situations in which the statute might be conceived to operate with unduly oppressive or unjustifiably arbitrary impact indicative of unconstitutionality. * * * [citing authority]."

Moorman as the challenging party has the burden to demonstrate that section 422.33(1)(b), already found to be generally constitutionally valid, violates the constitutional precepts invoked when applied to it because of special factual circumstances surrounding Moorman's claim for relief.

Under the record, Moorman has not carried its burden, since it has not demonstrated by the stipulated facts the Iowa single-sales-factor-apportionment formula constitutes an unreasonable and arbitrary application in Moorman's particular case. No unusual or special factual circumstances inherent in Moorman's corporate operations are shown to exist. All that is established by the record is that Moorman apparently functions in a manner not dissimilar from the typical unitary business organization. No evidentiary justification is provided for a conclusion Moorman is somehow different from those corporations legitimately subject to the provisions of section 422.33(1)(b). In the absence of such evidence Moorman has not made out a sufficient case for overturning on constitutional grounds the application of the Iowa single-sales-factor formula to its net income.

VI. Article VIII, section 12, of the Iowa Constitution is applicable to corporations and provides as follows:

"Subject to the provisions of this article, the General Assembly shall have power to amend or repeal all laws for the organization or creation of corporations, or granting of special or exclusive privileges or immunities, by a vote of two-thirds of each branch of the General Assembly; and *no exclusive privileges, except as in this article provided, shall ever be granted.*" (Emphasis supplied).

Moorman directs this court's attention to the parties' stipulation which demonstrates that one foreign manufac-

turing corporation was permitted to use an alternative apportionment formula during the years in question. This approval by the Director of a formula other than the sales-factor formula prescribed in section 422.33(1)(b), allegedly amounts to the unauthorized grant of an exclusive privilege in violation of the above constitutional provision.

Moorman's contention is without merit. It is clear from the language of the constitutional provision in question that it applies to legislative enactments. Consequently, it has no application to alleged improprieties on the part of the Director. However, this should not be understood as assigning unfettered discretion to the Director. The general principles embodied in the constitutional provision are well covered by various other constitutional guarantees which are applicable to the Director's conduct.

VII. Moorman's next contention focuses upon the Director's failure to permit Moorman to utilize an alternative apportionment formula. It is argued the Director's rejection of Moorman's request was arbitrary and capricious and contrary to the provisions of section 422.33(2) which provides:

"If any taxpayer believes that the method of allocation and apportionment hereinbefore prescribed, as administered by the director and applied to his business, has operated or will so operate as to subject him to taxation on a greater portion of his net income than is reasonably attributable to business or sources within the state, he shall be entitled to file with the director a statement of his objections and of such alternative method of allocation and apportionment as he believes to be proper under the circumstances * * *; and if the director shall conclude that the method of allocation and apportionment theretofore employed is in fact inapplicable and inequi-

table, the director shall redetermine the taxable income by such other method * * * as seems best calculated to assign to the state for taxation the portion of the income reasonably attributable to business and sources within the state, not exceeding, however, the amount which would be arrived at by application of the statutory rules for apportionment."

The tenor of Moorman's argument concerning the Director's allegedly arbitrary and capricious conduct makes it impossible to separate this issue from the previous issues concerning the constitutionality of section 422.33(1)(b). Moorman's argument herein is based upon the constitutional invalidity of the sales-factor apportionment formula and, once again, relies almost exclusively upon General Motors Corp. v. District of Columbia, supra.

By reason of the determinations made in the previous divisions of this opinion we conclude Moorman's contention considered in this division is without merit.

The decisions reached in divisions II, III and IV of this opinion require a reversal upon the Director's appeal. By reason of the determinations reached in divisions V, VI and VII the matter is affirmed on Moorman's cross appeal.

All Justices concur except McCormick, J., who concurs specially.

McCORMICK, J. (concurring specially).

The United States Supreme Court has not yet decided the constitutionality of a corporate income tax formula which apportions net income of a unitary corporation based solely on the geographical distribution of sales. Although the Court has said "the geographic distribution of a corporation's sales is, by itself, of dubious significance in

indicating the locus [of either a corporation's sources of income or the social costs which it generates]," it has expressly refrained from taking "any position on the constitutionality of a state income tax based on the sales factor alone." However, the Court has noted "the factors alluded to by this Court in justifying apportionment measures challenged in the past lend little support to the use of an exclusively sales-oriented approach." General Motors Corporation v. District of Columbia, 380 U.S. 553, 561, 85 S.Ct. 1156, 1161, 14 L.Ed.2d 68, 73-74 (1965). In view of these statements by the Supreme Court in its most recent case touching on the subject, it seems reasonable to conclude that the constitutionality of Iowa's apportionment formula is open to question.

Moreover, I do not believe the *General Motors* case is wholly distinguishable on the basis suggested by the majority. Nevertheless, I agree with the majority that the case is not dispositive of the constitutional issues we face in this case. Further, under existing precedent of the Supreme Court and this court, I agree that Moorman did not establish the unconstitutionality of the Iowa apportionment formula either on its face or as applied here under the state due process clause and the federal due process and commerce clauses. Finally, I do not agree with the Director's view of his duty under Code § 422.33(2) but do not believe he breached his duty under the present record.

I. The problem addressed by the Court in *General Motors* was one of statutory interpretation. Hence the case did not involve principles of constitutional adjudication which implicate not only the heavy burden which must be met in demonstrating invalidity of a statute but also the distinction between invalidity of a statute on its face and as applied. See United States v. Raines, 362 U.S. 17,

80 S.Ct. 519, 4 L.Ed.2d 524 (1960). A statute is not unconstitutional on its face unless it is unconstitutional in every conceivable state of facts; it is ordinarily not unconstitutional as applied unless it is unconstitutional as applied in the specific factual situation before the court. The significance of this distinction is reflected in the position of the dissenters in *General Motors* in the court of appeals. They did not dispute the constitutionality of the single-factor formula on its face. See District of Columbia v. General Motors Corporation, 336 F.2d 885, 902-904 (D.C. Cir. 1964); see also Smoot Sand and Gravel Corp. v. District of Columbia, 261 F.2d 758, 763 (D.C. Cir. 1958) (" 'And the gross receipts formula has been in operation too long and upheld in the courts too frequently to be attacked as unfair or unreasonable *per se* or in the abstract.' "). To be unconstitutional on its face the formula would have to be unconstitutional all of the time, not just some of the time.

In *General Motors*, the Supreme Court based its decision on resolution of the issue whether the district tax commissioners acted within their statutory authority when they adopted a single-factor sales formula to determine the portion of corporate net income subject to the franchise tax. Two statutory directives existed. One required that the tax be on the portion of net income " 'fairly attributable to any trade or business carried on or engaged in within the District * * *.' " The other provided that the net income derived from the trade or business of any corporation " 'carried on or engaged in both within and without the District * * * be deemed to be income from sources within and without the District.' " *General Motors*, supra, 380 U.S. at 554-555, 85 S.Ct. at 1157, 14 L.Ed.2d at 70. In holding that the single-factor formula was inconsistent with these statutory directives, the Court relied on the fact that the formula would not apportion income to

non-sales income-producing activities outside the District. By statutory mandate, net income from District sales had to be considered the product in part of outside sources. Yet the sales factor formula would not apportion any income outside the District if all sales were made in the District, even though manufacturing occurred elsewhere.

I do not believe the existence of the second statutory requirement wholly distinguishes *General Motors* from the present case on the theory this directive is not part of the constitutional standard. Of course, the first statutory requirement is identical to the constitutional mandate under the due process and commerce clauses that a tax be fairly apportioned to commerce carried on within the taxing jurisdiction. See Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450, 79 S.Ct. 357, 3 L.Ed.2d 421 (1959); Annot., 34 L.Ed.2d 749, 765. I believe the second requirement is part of the constitutional standard when non-sales income-producing activities do occur outside the taxing jurisdiction. For example, when manufacturing activity occurs outside the jurisdiction, I believe profit realized upon sale of the manufactured goods in the taxing jurisdiction must be deemed to arise from that activity as well as from the sale. This is as basic as the principle of contradictions. A stick cannot have only one end. Similarly, income cannot be isolated from the capital or labor, or both, which produce the product or service which is sold. This is a matter of self-evident fact rather than a matter of "economic theory" as suggested by the Director in this case.

This fact has been consistently recognized by the Supreme Court. See Stratton's Independence v. Howbert, 231 U.S. 399, 34 S.Ct. 136, 58 L.Ed. 285 (1913). It is basic to the apportionment formula cases. In Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 120, 41 S.Ct. 45, 47,

65 L.Ed. 165, 169 (1920), the Court observed, "The profits of the corporation were largely earned by a series of transactions *beginning with manufacture in Connecticut and ending with sale in other States.* (emphasis added). The challenge to the apportionment formula failed in *Underwood* because the taxpayer failed to demonstrate the apportionment formula, based on the geographical situs of real and tangible personal property, reached more than the profits actually earned by the income-producing activities in the taxing state. A different result occurred in Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell, 283 U.S. 123, 51 S.Ct. 385, 75 L.Ed. 879 (1931), precisely because the taxpayer did meet that burden. ("[T]he statutory method, as applied to the appellant's business for the years in question, operated unreasonably and arbitrarily in attributing to North Carolina a percentage of income out of all appropriate proportion to the business transacted by the appellant in that state.") 283 U.S. at 135, 51 S.Ct. at 389, 75 L.Ed. at 908. The constitutional standard is premised on the theory that each transaction from manufacture through sale contributes to the income which is realized, but it puts the heavy burden on the taxpayer to demonstrate what share of his income from a unitary corporation is attributable to activities in the taxing jurisdiction, and further, that the apportionment formula produces a grossly distorted result in those circumstances. *Id.*, 283 U.S. at 133, 51 S.Ct. at 389, 75 L.Ed. at 905 ("The difficulty of making an exact apportionment is apparent and hence, when the state has adopted a method not intrinsically arbitrary, it will be sustained until proof is offered of an unreasonable and arbitrary application in particular cases.").

Any single-factor formula is thus capable of producing a grossly distorted result because it focuses artificially on only one component of the corporation's income-produc-

ing activities. See, e.g., Norfolk and Western Railway Company v. Missouri State Tax Commission, 390 U.S. 317, 88 S.Ct. 995, 19 L.Ed.2d 1201 (1968). Less danger exists that a multiple-factor formula will have that result because it recognizes additional relevant components.

I believe the Supreme Court struck the single-factor sales formula in *General Motors* because it read the governing statute as requiring adoption by the commissioners of an apportionment formula which would never deny recognition to non-sales income-producing activities which occurred outside the District. The case is distinguishable from the present one because the constitutional standard does not demand as much. Instead, it prohibits use of an apportionment formula which, in a given case, grossly overstates the portion of net income attributable to income-producing activities in the taxing jurisdiction. While this standard makes a single-factor sales formula more susceptible to successful attack in a particular application—for example when all sales occur in the taxing jurisdiction and all manufacturing occurs in another jurisdiction—it does not make a single-factor sales formula unconstitutional in every conceivable circumstance nor does it relieve the taxpayer of his burden to prove unconstitutionality of its application.

In the present case, Moorman did not attempt to prove the amount of its actual net income from Iowa activities in the years involved. Therefore no basis was presented for comparison of the corporation's Iowa income and the income apportioned to Iowa under the formula. In this era of sophisticated accounting techniques, it should not be impossible for a unitary corporation to prove its actual income from activities in a particular state. However, Moorman showed only that its tax liability would be substantially less if Iowa employed a three-factor apportionment formula. We have no basis to assume that the three-factor formula produced a result equivalent to the corporation's actual income from Iowa activities. Having failed to establish a basis for comparison of its actual income in Iowa with the income apportioned to Iowa under the single-factor formula, Moorman did not demonstrate that the single-factor formula produced a grossly unfair result. Thus it did not prove unconstitutionality of the formula as applied.

II. We are not limited in our interpretation of the due process clause of Ia. Const. Art. I § 9 by interpretations of the same language in U.S. Const. Amend. 14 by the Supreme Court. Deference to federalism has led the Supreme Court to accord states wide latitude in economic matters. See New Orleans v. Dukes, 427 U.S. 297, 303, 96 S.Ct. 2513, 2516-2517, 49 L.Ed.2d 511, 516-517 (1976). This factor does not inhibit state courts applying similar state constitutional provisions. In addition, we have the independent right to say what our state constitution means. See Brennan, *State Constitutions and the Protection of Individual Rights*, 90 Harv. L. Rev. 489 (1977). However, the distinction makes no practical difference in the present case because we have accorded equivalent latitude to the legislature in tax matters under our state constitution. See City of Waterloo v. Selden, 251 N.W.2d 506 (Iowa 1977).

III. I do not believe Moorman's attack on the single-factor apportionment formula is answered by the Director's reliance on the frequent statement of the Supreme Court that, because of the practical impossibility of a state's achieving perfect apportionment, a "rough approximation" is sufficient. See International Harvester Co. v. Evatt, 329 U.S. 416, 67 S.Ct. 444, 447, 91 L.Ed. 390, 395 (1947). This rule does not excuse a state from trying to achieve

fairness, nor does it excuse a state from using a different formula in situations where it is demonstrated that an existing formula grossly overreaches.

IV. Similarly, I do not agree with the Director that his power to grant relief under Code § 422.33(2) is limited to situations where application of the sales factor formula would be unconstitutional. I do not understand that the majority opinion approves this interpretation, but does not pass on it. I would disapprove it. The statute does not purport to impose upon the taxpayer a burden of proving unconstitutionality in order to obtain relief from the formula. Instead, he is merely required to file a statement of his objections and set forth "such alternative method of allocation and apportionment as he believes to be proper under the circumstances * * *." In turn, the Director is not precluded from affording relief except when the taxpayer proves a grossly distorted result will ensue from use of the sales formula. Rather he is empowered to grant relief when he finds the statutory formula "inapplicable and inequitable." The statute vests the Director with reasonable administrative discretion and manifests a legislative intention that it be exercised. No issue is presented in this case regarding the constitutionality of this delegation of power.

I do not believe Moorman was prejudiced by the Director's refusal to exercise this discretion in the present case because the record does not show Moorman made an adequate case for its exercise.

I concur in the result.

IN THE SUPREME COURT OF IOWA

Civil Appeal No. 2-60020

MOORMAN MANUFACTURING COMPANY
Plaintiff-Appellee,

vs.

G.D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant-Appellant

Appeal From the District Court
of Polk County
Hon. Anthony M. Critelli, Judge

APPELLEE'S PETITION FOR REHEARING

(Filed June 3, 1977)

COMES NOW the Plaintiff-Appellee-Cross-Appellant, Moorman Manufacturing Company (hereinafter referred to as Moorman) and following this Court's reversal of the District Court's rulings in favor of Moorman and the affirmance of the District Court's rulings adverse to Moorman by the decision of this Court entered May 25, 1977, respectfully urges this Court to grant Moorman a rehearing for the following reasons:

1. The Court should reconsider its decision that the Iowa single sales factor method of apportioning net income derived from the manufacture or sale of tangible personal property is not facially unconstitutional in violation of the due process clauses of the federal and Iowa Constitutions.

This Court appears to reject Moorman's arguments on the basis that "the constitution is not a formulary" and that single *property* factor methods of apportionment have been approved by prior decisions of the United States Supreme Court. Moorman agrees that thus far the United States Supreme Court has not imposed a single method of apportionment on the states. This, however, does not logically lead to the conclusion that *any* method of apportionment may be used with impunity by the states. Likewise, the approval of a single *property factor* method of apportionment does not automatically place that Court's imprimatur on the single *sales* factor method of apportionment.

It is undisputed that a method of apportioning a corporation's net income must reflect the distribution of either a corporation's sources of income or the social costs which it generates. In *General Motors Corp.* v. *District of Columbia*, 380 U.S. 553, 85 S. Ct. 1156, 14 L. Ed. 2d 68, the Supreme Court specifically found that the prior decisions of the Court approving single property factor apportionment formulae "lend little support to the use of an exclusively sales-oriented approach." 380 U.S. at 561. The fact that the *General Motors* case turned on statutory interpretation in no way vitiates the *reasoning* of that decision.

In *General Motors*, the Supreme Court used a hypothetical to demonstrate the fatal infirmities of the single sales factor apportionment method, yet this Court appears to require mathematical exactitude of the taxpayer when facial constitutionality is at issue. This Court's decision amounts to a finding that a unitary business cannot meet its burden of proof in demonstrating facial unconstitutionality unless it can show with particularity exactly how much income was a result of commercial activities outside

this state. This position is directly contradictory to the recognition by this Court that such a showing is *inherently impossible* in the case of a unitary business (see, e.g., p. 13 of the decision). Furthermore, facial unconstitutionality *must* be proven by the use of hypotheticals as was done in *General Motors*, where the facial invalidity of a regulation was at issue. In no other way can a litigant negative every reasonable basis which may support the statute. In the case before this Court, Moorman has proven the facial unconstitutionality of §422.33(1)(b) by the use of hypotheticals, none of which have been challenged.

In this case, the Court imposes a burden of proof which it acknowledges can never be met, with the consequence that a method of apportionment can never be proven unconstitutional on its face. This reasoning was unequivocally rejected by the Supreme Court in *General Motors*. When a method of apportionment is inherently improper, the taxpayer has no burden of proof to demonstrate that he has been wronged in constitutional terms. There is absolutely no legal justification for rendering a statute unconstitutionally impregnable on its face by imposing a burden of proof requirement that relates solely to that statute's application to the challenger.

2. The Court should reconsider its decision that the Iowa single sales factor method of apportioning net income derived from the manufacture or sale of tangible personal property is not facially unconstitutional in violation of the Commerce Clause of the United States Constitution.

This court accepts the principle that risk of multiple taxation is sufficient to render a method of apportionment facially unconstitutional (decision p. 28), but apparently finds that deductions allowed by Iowa statute preserve the Iowa method from unconstitutionality. Moorman con-

tends that this Court has confused the concept of tax *base* with the validity of the method of apportioning that base.

In determining the income to be subject to apportionment to Iowa, the state begins with net income per the federal income tax return, reduces it by items of income that it cannot constitutionally tax (e.g. income from federal securities) and increases it by items of income that the federal government does not tax (e.g. municipal interest) and by the Iowa income tax deducted on the federal return. The items of "passive income" (dividends, interest, rents and royalties) are then removed from this net income and *allocated* (not apportioned) either inside or outside the state. In addition, Iowa allows as a deduction from net income per federal return 50% of the taxpayer's federal income tax in determining the amount of net income to which the Iowa apportionment formula is to be applied (§422.35(4)).

This Court finds that since Iowa allows a deduction for 50% of the federal income tax, any inequity in the apportionment formula is thereby remedied. This is obviously false. The Iowa statute apportions *net* income. The legislature defines "net income" as it sees fit, subject to constitutional limitations, and varies the deductions allowable from time to time. (§422.35) For example, prior to 1967, the state allowed corporations a deduction for *100%* of their federal income tax liability (§422.35(4), Code of Iowa). If the Court's reasoning is correct, the validity of the apportionment formula changes as allowable deductions change. Following this argument, logically, if the apportionment formula were valid when *100%* of federal income tax was an allowable deduction in Iowa, it would have been less valid or invalid when such deduction was reduced to 50% of the federal income tax and would be

rendered *invalid* if the legislature should eliminate *any* deduction for federal income tax.

Likewise, assume a corporation with net income for federal tax purposes but no federal income tax liability because of allowable credits against tax, such as the investment credit. Is the Iowa apportionment formula invalid as to this corporation because it receives no federal tax deduction in computing its net income for Iowa purposes yet valid as to other corporations with a federal tax liability?

The foregoing irrefutably demonstrates that tax base (net income) and the method of apportionment are separate and independent factors. There is absolutely no logical or legally acceptable reason for justifying the apportionment formula by reference to the tax base. Consequently, the risk of multiple taxation does exist under the Iowa apportionment formula and the formula is thus violative of the Commerce Clause.

3. The Court should reconsider its decision that the Iowa single sales factor method of apportioning net income derived from the manufacture or sale of tangible personal property is not facially unconstitutional in violation of the equal protection guarantees of the federal and state Constitutions.

The Iowa method of apportionment differentiates between corporate manufacturers based on the location of their sales. The examples contained in Moorman's brief (pp. 25-27) demonstrate that such discrimination within the permissible classification of "corporations" is *inherent* in the statute. In fact, the Iowa legislature has recognized the discrimination inherent in §422.33(1)(b) by passing within the last month SF-140, which requires sales outside the state by Iowa farm corporations to be treated as Iowa sales for apportionment purposes.

Moorman contends that while it is permissible to separately classify corporations as distinguished from other classes of taxpayers, members of that class may not constitutionally be discriminated against. This Court's opinion sets forth no authority permitting members of a single class to be treated differently than other members of the same class. By its very terms, the method of apportionment in the Iowa statute does not have a uniform operation. It is not Moorman alone that carries an unfairly large tax burden in relation to services rendered by the State, but all out-of-state manufacturers. This is *facial* unconstitutionality at its worst.

4. The Court should reconsider its decision that the Iowa single sales factor method of apportioning net income derived from the manufacture or sale of tangible personal property is not unconstitutional as applied to Moorman.

In judging the facial constitutionality of the Iowa apportionment formula, a study of hypothetical situations is sufficient, as the United States Supreme Court recognized in *General Motors*. A determination of the constitutionality of the apportionment method as it applies to Moorman necessitates an analysis of Moorman's particular situation.

The parties stipulated a substantial amount of statistical information concerning Moorman during the years at issue. This information was analyzed by Moorman in its opening brief in great detail (Brief pp. 10-12; 16-19). This data demonstrates beyond question that the state of Iowa is taxing income partially created in Illinois, is causing actual, substantial multiple taxation to be visited upon Moorman and is placing a burden upon Moorman's interstate activities.

Nowhere in its opinion does this Court refute these unassailable conclusions derived from this stipulated statistical data. Yet the Court seems to indicate that Moorman has failed in meeting its burden of proof in this area. Moorman asserts (and the Court agrees) that by reason of the very nature of a unitary business it is impossible to assign each item of income and expense on a state-by-state basis. Indeed, the Iowa statute requires only that *net* income be apportioned. Moorman has placed in evidence via the stipulation sufficient relevant information to demonstrate the presence of the evils arising for the Iowa apportionment formula catalogued above.

It is submitted that if there is indeed *any* type or quantum of evidence sufficient to carry a taxpayer's burden of proof in this type of case, Moorman has more than fulfilled the requirements. As noted in the last paragraph on page 15 of the decision, the state must come forward with evidence to counter that provided by Moorman. This the state has failed to do.

We respectfully submit that this Court should reexamine the statistical evidence in light of our briefs. Whether Moorman is in a situation similar or dissimilar to other corporations is immaterial when the issue is constitutionality in *application*, for all that need be shown is that the State of Iowa is levying a tax on a greater portion of Moorman's net income arising from Iowa sales than is permissible under the federal and Iowa Constitutions. We believe that the answer must be resoundingly affirmative.

WHEREFORE, the Plaintiff-Appellee-Cross-Appellant, Moorman Manufacturing Company, respectfully prays the Court to grant it a rehearing in the above-entitled cause.

Respectfully submitted,

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ATTORNEYS' COST CERTIFICATE

We hereby certify that the costs paid for printing the foregoing Petition for Rehearing of Appellee-Cross-Appellant, Moorman Manufacturing Company was $.....

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IN THE SUPREME COURT OF IOWA

No. 2-60220

MOORMAN MANUFACTURING COMPANY,
Plaintiff-Appellee,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Defendant-Appellant.

ORDER

(Filed June 27, 1977)

Plaintiff-Appellee's petition for rehearing in the above entitled matter has been duly considered by the entire membership of the court and is now refused and denied.

Done this 27th day of June, 1977.

/s/ C. Edwin Moore
Chief Justice—Iowa Supreme Court

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IN THE SUPREME COURT OF IOWA

No. 2-60220

MOORMAN MANUFACTURING COMPANY
Appellee,
v.
G. D. BAIR, DIRECTOR OF REVENUE
STATE OF IOWA
Appellant.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

(Filed August 4, 1977)

Notice is hereby given that Moorman Manufacturing Company, the Appellee above-named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of Iowa reversing the rulings of the Polk County District Court in favor of Appellee and affirming the District Court's rulings adverse to Appellee entered in this action on May 25, 1977 and from the denial of Appellee's Petition for Rehearing entered on June 27, 1977.

This appeal is taken pursuant to 28 U.S.C. §1257(2).

/s/ Walter R. Brown
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Supreme Court, U. S.
FILED
OCT 20 1977
MICHAEL RODAK, JR., CLERK

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1977

NO. 77-454

MOORMAN MANUFACTURING COMPANY,

Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE
STATE OF IOWA,

Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

MOTION TO DISMISS

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IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1977

NO. 77-454

MOORMAN MANUFACTURING COMPANY,

Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA

Appellee,

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

MOTION TO DISMISS

Appellee (Director) hereby makes a Motion to Dismiss this appeal of Appellant (Moorman) pursuant to United States Supreme Court Rule 16 for want of substantial federal questions and because the single sales factor apportionment formula contained in § 422.33(1)(b), Code of Iowa, 1975, does not violate the Constitution of the United States of America, Article I, Section 8, Clause 3 (Commerce clause), Constitution of the United States of America, Amendment XIV (Due Process clause), and Constitution of the United States of America, Amendment XIV (Equal Protection clause), either on its face or as applied to Moorman's net income.

OPINIONS BELOW

Copies of the opinions of the trial court are appended to Moorman's Jurisdictional Statement. The opinion of the Iowa Supreme Court entered on May 25, 1977, is reported at 254 N.W.2d 737 (1977). Copies of that opinion and order denying Moorman's petition for rehearing are appended to the Jurisdictional Statement.

JURISDICTION

Moorman invokes the jurisdiction of this court under 28 U.S.C. § 1257(2) since the Iowa Supreme Court held that the Iowa net income tax apportionment formula contained in § 422.33(1)(b), Code of Iowa, 1975, for reasonably attributing to Iowa a portion of Moorman's unitary net income derived from the manufacture or sale of tangible personal property by the ratio which gross sales made within Iowa bear to total gross sales, did not, on its face or as applied to Moorman's net income, violate the commerce clause and Due Process and Equal Protection clauses of the United States Constitution.

QUESTIONS PRESENTED

Whether the single-factor destination sales formula for the apportionment of net income prescribed by the Iowa income tax statute: (1) discriminates against interstate commerce through the device of multiple state taxation; (2) subjects to Iowa tax a corporation's income out of all reasonable proportion to the business transacted in Iowa; (3) constitutes the extraterritorial taxation of income; and (4) subsidizes exports and imposes a tariff on imports in violation of the Commerce clause and the Fourteenth Amendment's Due Process and Equal Protection clauses of the United States Constitution.

STATEMENT OF THE CASE

This case was presented to the Courts below upon a stipulation of facts. (R. Item 2, pp. 9-47). The only question on appeal to this Court concerns the constitutionality of the Iowa single sales factor net income apportionment formula.

Moorman, an Illinois Corporation, was engaged, during its fiscal tax years in question, March 31, 1968 through March 31, 1972, in the business of manufacture and sale of animal feeds. Such feeds were manufactured by Moorman in five plants located in Texas, Nebraska, and Illinois and sold by Moorman salesmen in more than 30 states. During the aforementioned fiscal years, Moorman carried on substantial income producing activities in the state of Iowa. After sales of feeds were negotiated by Moorman's Iowa sales force of over 500 employees, delivery to Iowa customers was typically made from one of six warehouses operated by Moorman in Iowa. Moorman engaged in no manufacturing in Iowa and the products sold to Iowa customers were all manufactured in Illinois. For the years in question, Moorman filed Iowa income tax returns, apportioning income to Iowa upon the basis of a three factor formula, consisting of sales, property, and payroll factors, computed by it.[1] For the years in question, the Director recomputed Moorman's Iowa apportionable net income by application of the Iowa sales factor formula, rather than the three factor formula computed by Moorman. After notice and opportunity for hearing, the tax assessments which are the subject of this appeal were confirmed by the Director. (App. A, pp. A1-47--all references to the Appendix herein are to the Appendix contained in Moorman's Jurisdictional Statement).

---

1. In its Jurisdictional Statement, Moorman claims to have used the three factor formula contained in the Uniform Division of Income for Tax Purposes Act. The Uniform Act does contain a three factor formula with sales, property, and payroll factors. Moorman's invocation of the Uniform Act as the source of its formula is here both an innovation and irrelevant. Innovative because it has never been suggested in this case prior to the Jurisdictional Statement. Irrelevant because the Act is not uniformly interpreted by those states which have adopted it and is certainly not binding on states, such as Iowa, which have not adopted it.

Moorman appealed the Director's determination to the Polk County District Court. The constitutional issues presented to the District Court were stipulated. (R. Item, 2, pp. 16-19).

The District Court held that the Iowa sales formula, on its face, violated the Commerce and Due Process, but not Equal Protection, clauses of the United States Constitution. (App. B, p. A40). In reaching these conclusions, the District Court stated that "no evidence beyond that in the stipulation was presented or is considered." (App. B, p. A9). The only evidence in the stipulation upon which the District Court predicated its factual findings causing it to conclude that the Iowa formula was facially unconstitutional consisted of a showing that a three factor formula as computed by Moorman would result in a lower percentage of net income apportionable to Iowa than would the Iowa single sales factor. (App. B., pp. A27-A28,A35-A36). This evidence, together with the District Court's unfounded assumption that Iowa taxed 100% of Moorman's net income from Iowa sales, caused the Court to conclude that, based upon the interplay of the Iowa and Illinois apportionment formulae only, the percentage of Moorman's 1968 net income actually taxed was 141.76% and similar conclusions were reached for the other tax years. (App. B, p. A36). The District Court was of the view that the constitutionality of the Iowa apportionment formula could be analyzed solely in terms of abstract computations of a three factor fomula and Iowa single factor formula. (App. B, pp. A27-A28, A35-A36). The District Court assumed that an apportionment formula is facially unconstitutional if it does not provide for geographical distribution of labor and capital, thus reading into the Constitution a preference for an equally weighted three factor property-sales-payroll formula to the exclusion of other formulae. [2] (App. B, pp. A32-A33). The nature of Moorman's unitary income producing activities in all states, the

2. On page 19 of its Jurisdictional Statement, Moorman adopts the District Court's Opinion as to Due Process and Interstate Commerce.

profitability of its operations in all states, the precise jurisdictional sources of Moorman's net income in all states, and Moorman's net income tax base computations in all states were simply never considered by the District Court in making its findings and conclusions. Prior constitutional apportionment precedents, with their appropriate constitutional principles, were deemed insignificant by the District Court. (App. B, p.A37). The District Court based its facial unconstitutionality holding upon *General Motors Corporation v. District of Columbia*, 380 U.S. 553 (1965), despite the fact this Court expressly noted that such case was not decided on constitutional grounds. (App. B, pp.A29, A37).

An additional Commerce Clause violation was found by the District Court based upon a hypothetical situation which assumed that the interplay between the Iowa and Illinois apportionment formulae gave the Iowa-based manufacturer a commercial advantage. (App. B, p. A38). Such a finding was inconsistent with the District Court's initial statement to only consider the evidence in the stipulation. (App. B, p. A9). As noted, infra, hypotheticals form no grounds for resolution of constitutional questions. Moreover, the conclusion here was inconsistent with the District Court's own determination that the equality of treatment of Iowa and non-Iowa corporations explained why the Iowa tax law was not in violation of the Equal Protection clause. (App. B, p. A24).

The Director appealed the District Court's decision to the Iowa Supreme Court, and Moorman cross-appealed. The Iowa Supreme Court unanimously reversed the District Court and held that the Iowa formula was facially constitutional and, further, that the formula was constitutional as applied to Moorman. (App. C, pp. A51-A89). Unlike the District Court, the Iowa Supreme Court noted that, for Due Process analysis, this Court's constitutional apportionment decisions recognize: (1) impossibility of achieving precise apportionment; (2) rough approximation is sufficient; (3) taxpayer's heavy burden in challenging apportionment formulae on constitutional grounds; and (4) the states are unrestricted in schoosing apportionment formulae and have great

leeway in making such choices. (App. C, p. A78). The Iowa Supreme Court noted that for the Iowa formula to be facially unconstitutional, it must fail to achieve constitutional standards "in every conceivable situation," but that this could not logically happen. (App. C, p. A79). The Court distinguished *General Motors Corporation v. District of Columbia*, supra, as expressly decided on nonconstitutional grounds, thus offering no precedent or support for facial invalidity of the Iowa sales formula. (App. C, pp. A76-A78). The Court noted that Moorman's evidence merely showed a larger percentage of total net income apportioned to Iowa by the Iowa single factor formula than by Moorman's computed three factor formula, but that such evidence formed no basis to infer "either double taxation or a taxation of extraterritorial values" in violation of Due Process. (App. C, p. A80).

The Due Process analysis along with the "potentially large deductions" in computation of the Iowa tax base were advanced as reasons by the Court for concluding that the Iowa formula did not facially violate the Commerce clause, the Court stating: "Clearly, a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales." (App. C, p. A82). In essence, the Iowa Supreme Court concluded that the so-called "findings of fact" of the District Court relied upon by Moorman in its Jurisdictional Statement herein were unjustified inferences, unsupported by the evidence, and were based upon unproven assumptions and improper analysis of the constitutional principles involved. (App. C, pp. A80, A82).

The Iowa Supreme Court also determined that the Iowa sales formula did not facially violate Equal Protection, pointing out that no evidence was introduced on this issue by Moorman which only attempted to show "extreme" hypothetical situations.[3] (App. C, p. A85). Thus, it was not shown, for Equal Protection

3. This same conclusion is justified as to Moorman's argument that such hypothetical condition violates Due Process or the Commerce Clauses. Consequently, no showing has been made that the Iowa sales formula somehow subsidizes exports and penalizes imports.

purposes, that the Iowa sales formula subsidizes exports and imposes a tariff on imports.

The Court determined that the tenor of Moorman's contentions that the Iowa sales formula was unconstitutionally applied to its net income, as ordered by the Director, was inseparable from its allegations as to facial constitutionality. (App. C, p. A86). Thus, having concluded the Iowa formula was facially valid, the Court held that Moorman had not carried its burden of showing that the Iowa formula was unconstitutionally applied to it. (App. C, pp. A86-87).

ARGUMENT

Moorman asserts that the Iowa sales formula contained in § 422.33 (1)(b), Code of Iowa, violates the Fourteenth Amendment's Due Process and Equal Protection clauses and the Commerce clause of the United States Constitution. Thus, federal questions have been raised, but are they substantial? Under 28 U.S.C. § 1257(2) a federal question is not substantial if it has been settled by previous decisions of this Court. *Zucht v. King*, 260 U.S. 174 (1922).

Moorman's Jurisdictional Statement clearly discloses a two-prong approach which is: (1).The Iowa sales formula is facially unconstitutional; and (2).The Court should approve, to the exclusion of any other apportionment formula, the three factor formula as contained in the Uniform Division of Income for Tax Purposes Act. Indeed, this approach by Moorman could not be more clearly set forth than it is in pages 20-23 of its Jurisdictional Statement. And, in attempting to show that the federal questions are substantial, in pages 12-19 of its Jurisdictional Statement, Moorman eschews any pretense that this Court should consider the application of the Iowa sales formula separately from its facial constitutionality.[4] In short, Moorman

4. This approach is consistent with Moorman's contentions, as noted by the Iowa Supreme Court, that the tenor of Moorman's constitutional assertions as to application of the Iowa sales formula could not be separated from its facial constitutionality arguments. (App. C, p. A86).

not only asserts the inherent invalidity of the Iowa sales formula, but in lieu thereof, this Court should force upon the States the equally weighted three factor formula as computed in the Uniform Act, rather than leave such a choice to appropriate legislative bodies.

Against this backdrop, previous decisions of this Court resolve, upon Due Process and Commerce clause grounds, the facial constitutionality of the Iowa sales formula. These decisions clearly disclose that this Court has never struck down, on constitutional grounds, a state tax apportionment formula on its face and this Court has refrained from singling out any particular apportionment formula to the exclusion of all others. The cases show that this Court has facially upheld, upon constitutional grounds, diverse apportionment formulae in the following cases: *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920) (single property factor); *Bass, Ratcliff & Gretton Ltd. v. State Tax Commission*, 266 U.S. 271 (1924) (single assets factor); *National Leather Co. v. Massachusetts*, 277 U.S. 413 (1928) (single property factor); *Hans Rees' Sons, Inc. v. North Carolina*, 283 U.S. U.S. 123 (1930) (single property factor);[5] *Kent-Coffey Mfg. Co. v. Maxwell*, 291 U.S. 642 (1933) (single property factor); *Norfolk & Western Railway Co. v. North Carolina*, 297 U.S. 682 (1936) (net operating revenue formula based upon mileage factor); *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939) (single gross receipts factor); *Butler Brothers v. McColgan*, 315 U.S. 501 (1942) (three factor sales-property-payroll formula); *International Harvestor Co. v. Evatt*, 329 U.S. 416 (1947) (Two factor gross receipts and property formula).

Taxpayers, in the above cases, posited arguments similar to Moorman as to facial constitutionality and, except for *Hans*

5. In *Hans Rees'*, this Court declared the North Carolina apportionment statute invalid *as applied* to the particular factual situation involved. Moorman has made no attempt to come forward with such an evidentiary showing as did the taxpayer in that case. Moorman has made no attempt to show its selling profit or manufacturing profit (if any) as did the taxpayer in *Hans Rees'*.

Rees', taxpayers' evidence in those cases was similar to Moorman's comparison of the percentages apportioned by the formula under attack and some other method. Thus, there is no reason to suggest that the instant case should be treated differently than its constitutional predecessors by this Court.

In *Underwood*, this Court stated:

> "The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut, and ending with sale in other states." (254 U.S. at 120)

Consequently, it is clear that this Court has recognized sales as an income producing activity and, thus, it is proper to apportion income by the geographical distribution of sales as a matter of constitutional law. See also *Ford Motor Co. v. Beauchamp*, supra. Thus, the instant case does not present a situation where an apportionment formula is based upon matters having nothing to do with income producing activities connected with Iowa nor are peculiar circumstances present. *Norfolk & Western Railway Co. v. Missouri Tax Commission*, 390 U.S. 317 (1968).

Even in *General Motors v. District of Columbia*, 380 U.S. 553 (1965) relied upon almost exclusively by Moorman to sustain its constitutional arguments, this Court expressly noted its historical constitutional position that "the Court has refrained from attempting to define any single appropriate method of apportionment."[6] Yet, Moorman wants this Court to make such an exclusive definition. "The Constitution is not a formulary." *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435, 444 (1940). Moreover, this Court in *General Motors* did not hold that the sales factor formula does not apportion net income as Moorman states in its Jurisdictional Statement.

In those cases where this Court upheld single factor formulae as well as in the three factor case of *Butler Bros*, supra, the

6. 380 U.S. at 561

Director demonstrated, without contradiction or refutation by Moorman, "the tax schemes involved therein were much more harsh than Iowa's corporate tax scheme."[7]

Thus, it is clear that the Iowa sales formula could not be facially unconstitutional since it cannot be demonstrated that such formula fails to meet constitutional standards "in every conceivable situation which might possibly arise."[8]

Finally, this Court will not consider the constitutionality of a net income apportionment scheme as an abstract proposition to resolve the constitutional issues raised in the instant Appeal. *Northwestern States Portland Cement Company v. Minnesota*, 358 U.S. 450, 463 (1959). "The delicate power of pronouncing an Act of Congress unconstitutional is not to be exercised with reference to hypothetical cases thus imagined." *United States v. Raines*, 362 U.S. 17, 22 (1960). This same statement would be true as to state legislation. Consequently, Moorman's attack on the constitutionality of the Iowa sales formula is inappropriate, as a matter of constitutional law, to the extent it relies upon hypothetical Iowa-based manufacturers exporting goods out of Iowa and alleged unfair competitive conditions and alleged penalties against imports. Such was the nature of Moorman's Equal Protection assertions in the Courts below, de-emphasized by Moorman upon this appeal, and such is part of Moorman's Due Process and Commerce clause contentions.

Thus, it is clear that the federal questions presented on this Appeal have been resolved by previous decisions of this Court and are not substantial. There is simply no basis for declaring the Iowa sales formula facially unconstitutional (or unconstitutional as applied on the basis of the record evidence in this case) and forcing upon all the States the three factor formula as computed under the Uniform Act. Hence, this Court should dismiss Moorman's Appeal.

7. App.C, p. A71; R.Item 3, pp. 14-19.
8. App. C, p. A79

Aside from the fact that the federal questions are not substantial, this Court should dismiss this Appeal because the Iowa Supreme Court correctly determined that the Iowa sales formula does not violate the Fourteenth Amendment's Due Process and Equal Protection clauses and Commerce clause of the United States Constitution.

The Iowa Supreme Court's analysis and resolution of the constitutional questions involved in the instant case were clearly correct whereas the District Court, upon which Moorman relies so heavily in its Jurisdictional Statement, did not follow the principles contained in the previous constitutional decisions, already cited herein, of this Court. Indeed, the District Court expressly disregarded such constitutional precedents and based its decision wholly on the nonconstitutional decision of *General Motors Corporation v. District of Columbia*, supra.[9] The following statements made by this Court are applicable to the instant Appeal and were adhered to by the Iowa Supreme Court:

> "The legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It therefore adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the state." *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 120-1.
>
> "There is no evidence in the record as to whether the company received any net income from its New York business, or the amount of the profit and loss on that business, if any, either considered separately or in connection with the manufacturing business carried on in Great Britain." *Bass, Ratcliff & Gretton Ltd. v. State Tax Commission*, 266 U.S. 271, 283 (1924)

9. App. B, p.A37.

"A finding that the statute, though fair upon its face, is oppressive toward the railway in its practical operation cannot rest upon so fragmentary and partial a showing of facts. We must bear in mind steadily that the burden is on the taxpayer to make oppression manifest by clear and cogent evidence." *Norfolk & Western Railway Co. v. North Carolina*, 297 U.S. 682, 688 (1936).

"We reject petitioner's contention that constitutionality of state taxation turns on so narrow an issue as whether local assets rather than local gross receipts are used in a taxing formula." *Ford Motor Co. v. Beauchamp*, 308 U.S. 331, 335 (1939).

"The fact of the matter is that appellant has not shown the precise sources of its net income of $1,149,677. If factors which are responsible for that net income are present in other states but not present in California, they have not been revealed." *Butler Bros. v. McColgan*, 315 U.S. 501, 509 (1942).

"Furthermore, this Court has long realized the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as those of appellant, and has declared that 'rough approximation rather than precision' is sufficient . . . Unless a palpably disproportionate result comes from an apportionment . . . this Court has not been willing to nullify honest state efforts to make apportionments." *International Harvestor Co. v. Evatt*, 329 U.S. 416, 422 (1947).

"We must be on guard against imprisoning the taxing power of the states within formulas that are not compelled by the Constitution but merely represent judicial generalizations exceeding the concrete circumstances which they profess to summarize."[10] *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435, 445.

The above constitutional precepts, consistently expounded by this Court over the years, were fully considered by the Iowa Supreme Court, but ignored by the District Court.[11] This Court has never held an apportionment formula unconstitutional for any form of state taxation, income or otherwise, upon the meager evidentiary showing presented by Moorman in the parties' stipulation. This Court's constitutional precedents require that Moorman, not the State of Iowa, come forward with evidence "clear and cogent" showing that the Iowa sales formula produced a "grossly distorted result" or an apportionment "out of all proportion to the business transacted" in Iowa.[12] Such a showing cannot be made, as a matter of constitutional law, by limiting the inquiry to a comparison of the apportionment percentages of the Iowa sales formula and Illinois three factor formula in the abstract, ignoring Moorman's income producing activities in all states, failing to consider or point out the profitability of Moorman's operations in all states, failing to point out the precise jurisdictional sources of Moorman's income in all states, failing to consider Moorman's tax bases computed for all states, assuming that an apportionment formula must give geographical consideration to capital and labor as a prerequisite for being facially valid, assuming that Moorman was taxed by the Iowa formula on 100% of its income derived from Iowa sales, and assuming by hypotheticals or hypothesis that the Iowa sales formula gives direct commercial advantages to Iowa-based companies and penalizes imports of foreign corporations. The Iowa Supreme Court clearly recognized that the District Court erred in making

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10. This statement by Justice Frankfurter is particularly apropos to the instant case where Moorman seeks a declaration of the Iowa sales formula's facial invalidity and its forced replacement by the Uniform Act's three factor formula.

11. App. C, pp. A78-A82

12. App. C, p. A79

its "findings" by recognizing such findings were not proven.[13]

In its Jurisdictional Statement, Moorman contends that the tax base is irrelevant. No real reason is given for such irrelevancy. Apportionment formulae do not operate in a vacuum and, until applied to a net income base, the percentages computed by such formulae would not disclose anything. Certainly, the tax base can be examined to determine if, as applied, a state has taxed to the extent of its constitutional authority. Moreover, the Iowa "operating incidence" of the tax in question is not on gross sales, as such, but upon *net* income. This net income figure is derived by subtracting from overall gross income various deductions, which for Iowa include a form of federal tax deduction. See § 422.35, Code of Iowa. Such deductions consist of expenses incurred in Iowa and other states by a unitary multistate business. Consequently, the tax base does have a bearing on whether Iowa did, in fact, tax 100% of Moorman's income derived from its Iowa sales. When the constitutional principles previously discussed herein together with the tax base are considered, it is clear that the Iowa

13. App C, pp. A78-A82. In its Jurisdictional Statement, Moorman contends that the Iowa Supreme Court made no direct response to the findings of the District Court. In constitutional apportionment cases, the Courts are only required to determine whether a taxpayer has proved the invalidity of the formula. The Iowa Supreme Court did hold that Moorman's evidence did not prove multiple or extraterritorial taxation of its net income by Iowa which, for example, the District Court found was 141.76% for 1968. (App. B, p. A36; App C, pp. A79-A80). It should also be pointed out that this 141.76% figure was based upon the *abstract* interplay between the Iowa and Illinois apportionment formulae where it was assumed that Moorman was taxed by Iowa on 100% of its income from Iowa sales which the Iowa Supreme Court found to be erroneous – a direct response to the District Court's findings. (App. C, p. A82). Indeed, for 1968, the abstract interplay between the Iowa and Illinois apportionment formulae only showed that Iowa taxed 21.88% of Moorman's income and Illinois taxed 41.76% of such income. (R. Item 2, p. 28; R. Item 6, p. 17) Of course, these figures do not take into account such matters as net income base, profitability of operations in both states, and Moorman's precise jurisdictional sources of income in more than 30 states it did business in. The point is that the evidence in the stipulation does not, in any aspect viewed, disclose that the Iowa formula is unconstitutional as alleged by Moorman.

Supreme Court was correct in determining that Moorman was not taxed on 100% of its income derived from Iowa sales.

Moorman, in its Jurisdictional Statement, relies upon *General Motors Corporation v. District of Columbia*, supra, as, in effect, reasoning that an income tax apportionment formula based upon sales alone is facially unconstitutional. However, a close reading of that case clearly discloses that this Court rendered its decision "without reaching the constitutional questions raised."[14] Consequently, as the Iowa Supreme Court pointed out, "language used in such a decision does not afford a satisfactory basis for determining a state statute unconstitutional on its face."[15] Thus, this Court's criticism of a single sales factor formula offers no support for finding such a formula facially invalid, where such criticism is within the context of interpreting a statute, in view of the constitutional principles which this Court would have had to consider *if* it had based its decision on constitutional grounds. These constitutional principles which would have been considered in *General Motors*, but which were not, would include those considered by the Iowa Supreme Court as set forth in the previous decisions of this Court.[16] When those principles are considered, it is clear that Moorman, upon this appeal, could not demonstrate either the facial invalidity of the Iowa sales formula or any invalidity as applied to it. Moreover, it is clear that this Court's decision in *General Motors* as described by the Iowa Supreme Court turned on "the Court's interpretation of this statutory phrase -- which has no analogue in the Iowa statute and can scarcely be found in the due process clause."[17] Consequently, this Court never determined that the sales formula in *General Motors*, in fact, produced a "grossly distorted result", an apportionment "out of all proportion to the business transacted," or unreasonable multiple state taxation — the constitutional standards of invalidity. And, this Court, in *General*

14. 380 U.S. at 555
15. App. C, p. A77.
16. App. C, pp. A77-A82
17. App. C, p. A78

Motors never intimated that hypotheticals could be used to demonstrate unconstitutionality of apportionment formulae.

Moorman, in its Jurisdictional Statement, contends that the Iowa Supreme Court misapplied Justice Frankfurter's oft repeated phrase from *Wisconsin v. J. C. Penney Co.*, supra, 311 U.S. at 444. (App. C, pp. A78-A79). However, the Iowa Court did not, as Moorman contends, conclude that an apportionment formula is fair merely because Moorman is taxable. What the Iowa Court actually held, upon Due Process grounds, was that the fiscal policy of the State of Iowa as expressed by the Iowa sales apportionment formula was rationally related to Due Process principles applicable to determine the facial constitutionality of such formulae in as much as "the taxing power exerted by this statute bears fiscal relation to the protection, opportunities and benefits given by the state."[18] Indeed, this Due Process standard was cited by this Court in the apportionment case of *Norfolk & Western Railway Co. v. Missouri Tax Commission*, supra, 390 U.S. at 325 (footnote 5) wherein the particular apportionment formula involved was facially declared valid, but was stricken as applied to the peculiar factual circumstances proven by the taxpayer and not rebutted by the State.

Recent decisions of this Court continue a trend of allowing the states great leeway in their taxation of interstate commerce. *Standard Pressed Steel Co. v. Department of Revenue*, 419 U.S. 560 (1975); *Complete Auto Transit, Inc. v. Brady*, 97 S. Ct. 1076 (1977). The acceptance of Moorman's position in the instant Appeal would reverse such trend and create a new doctrine of constitutional law, inhibiting without justification the states in the exercise of their fundamental power of taxation.

In attempting to show that the federal questions raised are "substantial as a matter of public importance", Moorman in its Jurisdictional statement sets forth "dire consequences" to the

18. App. C, p. A79

effect that the decision of the Iowa Supreme Court will destroy the "free trade" in this country and that Iowa, along with other states which have adopted unequally weighted three factor formulae, have shifted tax burdens to "foreigners." The Director does not agree with these sentiments expressed by Moorman. Moreover, there is no basis for the conclusion that the decision of the Iowa Supreme Court will destroy, in essence, the economy of this country or inhibit competition.[19] The fact of the matter is that Moorman has simply raised a political, not constitutional, question. In this regard, it is not irrelevant to note that Congress, in which the Commerce power is placed by the Constitution, has frequently addressed the question of providing for a uniform net income tax apportionment formula and each time has refused to impose upon the States the straitjacket demanded by corporations and others who are unable to find in the United States Constitution any provision to support the exclusivity of the formulae they espouse. See, *e.g.* S. 1245, 93rd Cong. 1st Sess. (1973); H. R. 1538, 92nd Cong., 1st Sess. (1971); H. R. 669, 95th Cong. 1st Sess. (1977).

The aforementioned arguments in support of facial constitutionality of the Iowa sales factor formula are also herein adopted for purposes of supporting the constitutionality of the Iowa sales formula as applied to Moorman's net income.

19. In *Kent-Coffey*, the apportionment scheme upheld apportioned 99.2% of taxpayer's net income to the taxing state. In *Underwood*, 47% of taxpayer's net income was apportioned to the taxing state and the apportionment scheme was upheld. There is no evidence that this Court's decisions in those cases somehow led to unfair competition and barriers to interstate commerce. Further, this Court has over the years upheld diverse apportionment formulae which results have not created an unhealthy national economy.

CONCLUSION

The Director respectfully requests this Court to sustain his Motion to Dismiss since this appeal does not present substantial federal questions for the reason that the questions sought to be raised have been resolved by previous constitutional decisions of this Court. In addition, it is submitted that the Iowa Supreme Court correctly determined, by application of the appropriate constitutional principles consistently expounded by this Court, that the Iowa sales formula for apportioning net income to Iowa is facially constitutional and constitutional as applied to Moorman's net income for the years in question.

Respectfully submitted,

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PROOF OF SERVICE

STATE OF IOWA, POLK COUNTY, SS:

I, Harry M. Griger, being first duly sworn, do on oath say that I served printed copies of the foregoing Motion to Dismiss on the 19th day of October, 1977, by depositing the same in the United States mails, with first class postage prepaid, addressed to the following named persons at the addresses shown:

40 copies to — The Hon. Michael Rodal, Jr.
Clerk, Supreme Court of the United States
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Subscribed and sworn to before me at Des Moines, Iowa by Harry M. Griger, this 19th day of October, 1977.

Jessy J. Metcalf
Notary Public, State of Iowa

Supreme Court, U. S.
FILED
DEC 27 1977
MICHAEL RODAK, JR., CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

BRIEF FOR THE APPELLANT

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In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

BRIEF FOR THE APPELLANT

Moorman Manufacturing Company appeals from the final judgment of the Supreme Court of Iowa reversing the decision of the trial court and confirming an assessment of additional income tax measured by the difference between income apportionment according to the standard three-factor formula and attribution of income entirely to the situs of customers.

OPINIONS BELOW

The opinion and order of the Iowa Director of Revenue dated December 17, 1974, is unreported (A. 2). The Findings of Fact and Conclusions of Law of the District Court of the State of Iowa in and for Polk County, Equity No. CE 3-1595, filed December 17, 1976, the revision thereof filed January 7, 1977 (entitled Ruling on Joint Motion

to Reconsider and Supplemental Findings), and that Court's Judgment and Decree are unreported (A. 56). The opinion and judgment of the Supreme Court of Iowa entered May 25, 1977, is reported at 254 N.W.2d 737 (Iowa, 1977). Copies of that opinion and the unreported order denying rehearing entered June 27, 1977 are in the Appendix (A. 103).

JURISDICTION

The judgment of the Supreme Court of Iowa became final with the entry on June 27, 1977 of the order denying rehearing. The jurisdictional statement was filed September 22, 1977 and probable jurisdiction was noted November 14, 1977, 46 U.S.L. Week 3317 (U.S. Nov. 14, 1977). The jurisdiction of this Court is conferred by 62 Stat. 929, 28 USC 1257(2), the issue being a state statute unconstitutional on its face and so applied as to burden unduly Moorman's interstate commerce, to deprive it of property without due process of law and to deny it equal protection of the laws, contrary to Art. I, Sec. 8, Cl. 3 of the Constitution of the United States relating to interstate commerce and to the due process and equal protection guaranties of the Fourteenth Amendment thereto.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Art. I, Sec. 8, Cl. 3 of the Constitution of the United States and the Due Process and Equal Protection Clauses of the Fourteenth Amendment thereto are set forth in Appendix A, p. A1, *infra*.

The pertinent sections of the Code of Iowa, being Sections 422.33 and 422.35 contained in Volume II pages

1669 and 1670, Code of Iowa (1966) are set forth verbatim in Appendix B, pp. A1-A5, *infra*.

The pertinent section of the Illinois Income Tax Act, being 120 Ill. Rev. Stat. §3-304(a), is set forth verbatim in Appendix C, pp. A5-A6, *infra*.

The pertinent sections of the Uniform Division of Income for Tax Purposes Act §§3, 9, are set forth verbatim in Appendix D, p. A6, *infra*.

QUESTIONS PRESENTED[1]

Interstate Commerce, Due Process, Territorial Jurisdiction and Equal Protection

Whether the single-factor destination sales formula for the "apportionment" of net income, prescribed by the Iowa income tax statute, is invalid:

(a) as repugnant to the Commerce Clause of the Constitution;

(b) as repugnant to the Due Process Clause of the Fourteenth Amendment to the Constitution;

(c) as unconstitutionally extending the power of the State beyond its territorial jurisdiction;

(d) as repugnant to the Equal Protection Clause of the Fourteenth Amendment to the Constitution;

when the application of such formula results in the taxation by Iowa of 100% of the net income of a foreign corporation derived from that segment of its business consisting of the manufacture of products without Iowa and their sale to customers within Iowa, while a domestic

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1. Reprinted verbatim from Jurisdictional Statement.

corporation pays no Iowa income tax with respect to its exports, thus

(1) discriminating against interstate commerce by imposing upon it cumulative tax burdens (double taxation) to which local commerce is not subject;

(2) subjecting to Iowa tax an amount of income out of all reasonable proportion to the business actually done within Iowa;

(3) taxing extra-territorial values and assigning to Iowa values which belong to, and have been properly taxed by, another state (Illinois); and

(4) subsidizing exports and imposing a tariff on imports.

STATEMENT OF THE CASE

The operative facts were fully stipulated (A. 20), the sole issue on appeal being the constitutionality of the Iowa statute applied to those facts.

Moorman Manufacturing Company is an Illinois corporation headquartered in Quincy, Illinois. Its business is the manufacture of animal feeds which it sells to farmers and others in thirty states, including Iowa. During the years at issue, all goods sold to Iowa customers were manufactured in Illinois and no manufacturing was done in Iowa. Orders are solicited from Iowa customers by a substantial force of resident salesmen and typically are filled from stocks in warehouses in Iowa to which they have been shipped from factories in Illinois.[2]

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2. Moorman also made sales in Illinois which were delivered to Iowa. These were treated as Iowa sales under the statute in effect during the last year at issue and included in the controverted assessment (A. 3).

Appellant brought proceedings before the Iowa Director of Revenue for review of income tax deficiencies for the taxable years 1968 through 1972 assessed by him pursuant to the income tax section (Sec. 422.33) of the Code of Iowa. The Director affirmed the assessments. Moorman then appealed to the District Court, where there was trial *de novo*. The District Court found the statutory "apportionment" formula "facially unconstitutional" and struck most of the assessments (all that are involved in this Appeal). The Supreme Court of Iowa reversed the District Court and reinstated the assessments.

The assessments under Appeal are the differences between what Moorman paid, following the three-factor formula of the Uniform Division of Income for Tax Purposes Act, and the amounts asserted by the Director following the Iowa statutory single-factor formula of sales attributed to destination. The assessments tax 100% of Moorman's income from that segment of its business which consists of manufacturing goods in Illinois and selling them to customers in Iowa, taking no account of the contribution of capital and labor to the production of income.

The District Court found as *facts*: The Iowa single-factor formula taxed 100% of the income from each dollar of sales of Moorman's goods into Iowa, although 75% of payroll and 30% of capital are used in the manufacture of the goods (in Illinois) (A. 76); the Iowa formula fails to reasonably apportion profits traceable to Illinois and taxes activities occurring in Illinois (A. 77); the Iowa formula produces multiple taxation of the same income (A. 86); Illinois taxed the relevant income by the three-factor formula (A. 81); the Iowa formula taxed values beyond those which may be justly allocated to intrastate activity, and resulted in "gross overreaching" by the State

(A. 81); for 1968, the Iowa and Illinois formulae taken together "apportioned" 141.76% of Moorman's income from its Iowa sales (A. 84); Iowa is the only state attributing income to sales alone (A. 85); the interplay of the Iowa and Illinois formulae would give unfair advantage to an Iowa manufacturer selling in Illinois in that only one-third of the relevant income would be taxed (A. 86).

While Iowa was thus assessing 100% of the income arising from manufacture in Illinois and sale to Iowa customers pursuant to its destination-sales-only formula, Illinois was applying its three-factor formula of property, payroll and sales, equally weighted, to Moorman's net income for the same years (1970-1972). Since all manufacturing took place in Illinois, the property and payroll factors attributed to Illinois substantial parts of the same income that Iowa attributed entirely to itself—a clear case of double taxation.

The District Court held, on the basis of those findings, that Iowa's single-factor formula violated the Commerce and Due Process provisions of the United States Constitution, and cancelled the assessments (A. 40, 41). Upon appeal, the Supreme Court of Iowa reversed.

The Iowa Supreme Court's opinion makes much of the point that an apportionment formula cannot be precise and hence approximation is all that is required (A. 130). It asserts that a number of decisions of this Court approve single-factor formulae, without noting that none of them was anything like *this* single-factor formula (A. 124). It quotes extensively from *General Motors Corporation* v. *District of Columbia,* 380 U.S. 553 (1965), but dismisses that case as a statutory, rather than a constitutional, decision (A. 128), incidentally pointing out that the Iowa statute contains no provision that income from interstate

commerce shall be "deemed to" arise in both states (as the D. C. statute does), and says there is no due process requirement for such "deeming" (A. 130).

It asserts that evidence does not establish either double taxation or taxation of extra-territorial values—ignoring the findings of fact (A. 132). It denies that the assessments tax 100% of Moorman's income from Iowa sales because of statutory adjustments to the income *base* —thus relying upon an aspect of the tax law wholly irrelevant to apportionment, to conclude that Moorman had not show that its income from Iowa sales had been taxed more than 100%, again ignoring the findings of fact (A. 134).

The assessments were on a basis identical to that declared invalid in *General Motors Corporation* v. *District of Columbia, supra.* It was stipulated by the parties that if that basis is unconstitutional, the appropriate basis is the Uniform Act by which Moorman paid initially (A. 31).

The constitutional questions were presented and vigorously argued, both orally and in writing, at every opportunity and were considered by each of the three tribunals: the administrative proceeding, the district court in the trial *de novo,* and the Iowa Supreme Court, as shown by their respective opinions (A. 2, 56, 103). The questions raised, in each case contending invalidity under the pertinent provisions of the United States Constitution, of the statute both on its face and as applied, were: denial of equal protection; denial of due process; and undue burden on interstate commerce.

SUMMARY OF ARGUMENT

1. When two jurisdictions use overlapping formulae for the attribution of income for tax purposes, double taxation inevitably results, in violation of the Commerce Clause of the Constitution. When one of the jurisdictions applies the standard three-factor formula, the double taxation is the fault of the other jurisdiction.

2. The purpose and effect of the sales factor is to subsidize exports and impose a tariff on imports. It does not apportion income, but merely identifies the total income from the relevant segment of the business. When such income is derived in substantial part from activities outside the jurisdiction, the effect is to project the jurisdiction's reach beyond its geographical limits in violation of the Due Process Clause of the Constitution and in defiance of a fundamental principle of federalism.

3. The effect of the interplay of Iowa's sales-only formula with the three-factor formula used by other states, including Illinois, is to provide benefits to Iowa-based business unavailable to other business and hence deprives such other business, including Moorman, of its constitutional right to Equal Protection.

4. Even if it were not invalid on its face, the Iowa formula is invalid as applied to Moorman.

5. The economic impact of the Iowa decision, if allowed to stand, will be severe and will go a long way toward weakening the common market intended by the Constitution.

ARGUMENT

I. Double Taxation and Discrimination Against Interstate Commerce Violate the Commerce Clause.

> "The great majority of States imposing corporate income taxes apportion the total income of a corporation by application of a three-factor formula which gives equal weight to the geographical distribution of plant, payroll and sales. The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which sales are made will allocate 100% of the income to themselves." *General Motors Corporation* v. *District of Columbia*, 380 U.S. 553 (1965), at 559.

The commerce clause (Article I, Section 8, Clause 3) of the United States Constitution prohibits a state from imposing a tax which discriminates against interstate commerce either by providing a direct commercial advantage to local business or by subjecting interstate commerce to the risk of multiple taxation. *J.D. Adams Mfg. Co.* v. *Storen*, 304 U.S. 307 (1938); *Gwin, White & Prince* v. *Henneford*, 305 U.S. 434 (1939); *Evco* v. *Jones*, 409 U.S. 91 (1972). The Court recently emphatically and unanimously reaffirmed the commerce clause prohibition against tax discrimination in favor of home based businesses in *Boston Stock Exchange* v. *State Tax Commission*, 429 U.S. 318 (1977):

"Permitting the individual States to enact laws that favor local enterprises at the expense of out-of-state businesses 'would invite a multiplication of preferential trade areas destructive' of the free trade which the Clause protects."

All the income of a corporation, including that generated by interstate commerce, may be taxed (cumulatively) by the several states, but such income is not to be taxed twice. It is beyond question that a state in which a product is manufactured has the right to tax income arising from that product, even though it is sold in another state. This is true for at least two reasons:

1. The property (plant, equipment, raw materials, etc.) and people (employees) involved in the manufacture of the product are obviously part of the income-producing process; and

2. The state of manufacture renders services to the property and people involved in the manufacturing process.

Where, however, the state in which the sale occurs (Iowa) taxes *all* the income arising from the manufacture and sale, the taxpayer is subject to the risk of being taxed on more than 100% of the income, since the state of manufacture is likewise entitled to tax at least part of the income.

In this case, the overlap is less than the 67% noted by this Court in *General Motors* because Moorman has property and payroll in Iowa, and those amounts are excluded from the property and payroll which Illinois attributes to itself. In each of the five years in issue there is, however, very substantial overlap.

By applying the Iowa formula to Moorman's total apportionable income, the Director has determined the amount of Moorman's total net income resulting from the manufacture and sale of its products to Iowa customers. Pursuant to the Iowa single sales factor formula, all of the above income is taxed by the State of Iowa. However, since all the products sold in Iowa are produced in Illinois, that state is also entitled to tax the income resulting from sales in Iowa and in fact does so. Illinois uses an equally-weighted three-factor (payroll, property and sales) formula of apportionment. Illinois Income Tax Act, 120 Ill. Rev. Stat. §3-304(a) (App. C, pp. A5-A6). Pursuant to that (customary) formula, the Illinois property and payroll factors are determined by comparing property and payroll in Illinois with property and payroll everywhere. The sales factor in a three-factor formula such as that used by Illinois, relates principally to sales made in the taxing state (here, Illinois). Since we are concerned solely with the income arising from sales in Iowa, the sales factor in the Illinois formula will be zero.

Thus, the State of Illinois would tax income arising from sales in Iowa based upon the following percentages as determined above:

	FYE 3-31-68	FYE 3-31-69	FYE 3-31-70	FYE 3-31-71	FYE 3-31-72
Sales Factor (Sales in Iowa)	–0–	–0–	–0–	–0–	–0–
Payroll[3] Factor	41.00%	40.78%	41.16%	40.85%	40.87%
Property[4] Factor	84.29%	83.80%	61.99%	62.68%	70.15%
Total	125.29%	124.58%	103.15%	103.53%	111.02%
Average (Total ÷ 3)	41.76%	41.53%	34.38%	34.51%	37.01%

The "average" figure shown immediately above is the percentage of income arising from sales in Iowa that the state of Illinois would tax pursuant to its three-factor formula.

The total income derived from the manufacture and sale of goods to Iowa customers, as determined by the Director, is shown in the first line of the following tabulation.[5] Since Iowa taxes all of that, while Illinois taxes the shown percentages of the same income, the following degrees of overlap are established:

3. See Exhibit 15 to the Stipulation (A. 54).
4. See Exhibit 16 to the Stipulation (A. 54).
5. See Exhibit 8 to the Stipulation (A. 33).

	FYE 3-31-68	FYE 3-31-69	FYE 3-31-70	FYE 3-31-71	FYE 3-31-72
Income From Iowa Sales	$1,548,284	$1,632,469	$1,796,769	$1,837,533	$1,842,615
Total % Subject To Tax	141.76%	141.53%	134.38%	134.51%	137.01%
Total *amount* subject to tax	$2,194,847	$2,310,433	$2,414,498	$2,471,666	$2,524,567

This resulted in actual double taxation to the extent of $617,729 income in 1970, $634,133 in 1971 and $681,952 in 1972. Moorman's income from sales to Iowa customers in 1968 and 1969 was taxed 100% by Iowa but was not taxed by Illinois, which had no income tax in those years. However, Illinois could have taxed such income, as it did in the later years, and Iowa therefore exposed Moorman to the *risk* of double taxation which is enough to violate the Commerce Clause, it being irrelevant that Illinois did not choose to exert its full power of taxation.[6] *Gwin, White & Prince* v. *Henneford*, 305 U.S. 434 (1939); *J. D. Adams Mfg. Co.* v. *Storen*, 304 U.S. 307 (1938); *Evco* v. *Jones*, 409 U.S. 91 (1972).

The Iowa Court denies that Iowa taxes 100% of the income because deductions from gross income are allowed

6. This principle is recognized in the Uniform Division of Income for Tax Purposes Act, which assigns sales to destination in any jurisdiction in which the taxpayer is "taxable", without regard to whether it is in fact taxed (App. D, p. A6).

in computing net income. That argument is wholly specious, since neither base nor rate, although related to each other, has anything to do with apportionment. First the taxable income (the base) is determined according to statutory definition—gross, net, something between,—then the portion arising in the jurisdiction is found, and then the rate is applied to that portion. Base and rate are reciprocals. If there is a large base, such as gross receipts, the rate is usually low; if there is a small base, such as narrowly defined net income, the rate is apt to be high (in this case, 8% to 10%). But the definition of taxable income has no bearing whatever on what part of it belongs to what state. Iowa has taxed 100% of Moorman's relevant income as the Iowa statute defines "income". The fact that the definition is narrow and might have been broader is wholly irrelevant. It might have some relevance to an argument about rate, but there is no such question here, the sole issue being location.

The Iowa court says that since Iowa allows a deduction for 50% of the federal income tax, the formula does not tax all the taxable income. This is an obvious non sequitur. The Iowa statute divides *net* income. The legislature defines "net income" as it sees fit, subject to constitutional limitations, and varies the deductions allowable from time to time. (§422.35). For example, prior to 1967, the state allowed corporations a deduction for 100% of their federal income tax liability. (§422.35(4), Code of Iowa). If the Iowa court's reasoning is correct, the validity of the formula changes as allowable deductions change. Following this argument logically, if the formula were valid when 100% of federal income tax was an allowable deduction in Iowa, it would have been less valid or invalid when such deduction was reduced to 50% of the federal income tax and would be rendered invalid if the legislature should eliminate all deduction for federal income tax.

Likewise, assume a corporation with net income for federal tax purposes but no federal income tax liability because of allowable credits against tax, such as the investment credit or foreign tax credit. Is the Iowa apportionment formula invalid as to this corporation because it receives no federal tax deduction in computing its net income for Iowa purposes yet valid as to other corporations with a federal tax liability?

Finally, it must be remembered that *all* corporations, both foreign and Iowa, are allowed this deduction—it is not limited merely to non-Iowa based taxpayers.

The foregoing irrefutably demonstrates that tax base (net income) and the method of apportionment are separate and independent factors. There is absolutely no logical or legally acceptable reason for justifying an apportionment formula by reference to the tax base. Consequently, the risk of double taxation does exist under the Iowa formula, double taxation actually occurred, and the formula is thus violative of the Commerce Clause.

The purpose and effect of a "destination sales factor" is to subsidize exports and impose a tariff on imports. It does not "apportion" income, but merely identifies the income from that segment of the business which consists of manufacturing in one jurisdiction and selling to customers in another.

Relying on it alone, while other states use the standard formula, results in discrimination against interstate commerce. The Iowa statute serves to grant Iowa-based manufacturers a substantial advantage against competition from out-of-state manufacturers by increasing the latter's costs through subjecting them to multiple taxation. As shown previously in this brief, Moorman would be taxed on approximately 137% of its income from Iowa sales

during its fiscal year ended March 31, 1972, because of the single sales factor formula. However, any competitor of Moorman's which manufactures its products in Iowa would be subject to tax on only 100% of its income arising from Iowa sales. Thus, Moorman is at an immediate disadvantage in this situation solely by reason of the Iowa formula.

It has frequently been said, as the Director of Revenue said in this case, that "the use of formulae by other states where the taxpayer does business is not relevant." (A. 7). The thread of that argument is that we do it our way, they do it their way, and it doesn't matter that the taxpayer is squeezed; besides, our way is the right way and any unfairness is the fault of the other fellow.

This Court holds otherwise. It has frequently stated that double taxation puts an unconstitutional burden on interstate commerce and has acted to prevent it. In doing so, it has necessarily determined which jurisdiction was offending. While *General Motors, supra,* is the most pertinent of such decisions, there are others: e.g., *Freeman* v. *Hewit,* 329 U.S. 249 (1946); *Michigan-Wisconsin Pipe Line Co.* v. *Calvert,* 347 U.S. 157, 170 (1954); *Gwin, White & Prince* v. *Henneford,* 305 U.S. 434 (1939).

As indicated in the above quotation from *General Motors,* since almost all other states use the three-factor formula the responsibility for the double taxation is Iowa's. The reason, of course, is that the Iowa formula gives no credit to the contributions of capital and labor whereas other jurisdictions do. Therefore, Iowa's single factor sales formula imposes an unconstitutional discrimination on interstate commerce.

In considering these matters of double taxation of and discrimination against interstate commerce it is well to

keep in mind the reason for the Commerce Clause in the Constitution:

> ". . . every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation, that no home embargoes will withhold his exports, and no foreign state will by customs duties or regulations exclude them. Likewise, every consumer may look to the free competition from every producing area in the Nation to protect him from exploitation by any. Such was the vision of the Founders; such has been the doctrine of this Court which has given it reality. . . ." *H. P. Hood & Sons* v. *Dumond,* 336 U.S. 525, 538, 539 (1949). Quoted with approval in *Hughes* v. *Alexandria Scrap Corp.,* 426 U.S. 794, 808 (1976).

II. The Sales Factor Is Illegitimate As a Violation of Due Process and the Principle of Federalism.

The only rationale for taxes is governmental services, and in the case of business taxes the services to business, including such things as police and fire protection, roads and similar facilities, schools and others. *Northwestern States Portland Cement Co.* v. *Minnesota,* 358 U.S. 450 (1959). Business taxes should therefore be paid to the jurisdictions which provide those services to the particular business paying the taxes. Property taxes, for example, do just that. So do, though less clearly, payroll taxes. It is difficult on the basis of social costs to rationalize business income taxes—the losing business imposes just as much burden on governmental facilities as does the profitable one. Business income taxes must be accepted, but in determining to what jurisdictions they are to be paid the fundamental justification for any tax must be given effect.

The jurisdictions which have rendered services to a multistate business are all of them in which it carries on business; and the degree of such services in each jurisdiction is proportional to the business activity. Police and fire protection relate to property; schools and hospitals relate to employees. So if relative quantities of property and employees are measured, and that relationship applied to tax base, the taxes are apportioned according to the grounds for their justification: governmental services. The location of the business's customers, as such, is completely irrelevant.

Current fiscal thinking by most states, however, disregards the relationship between governmental services and payment (taxes) therefor. It is this disregard which supports business income taxes. Nevertheless, the logical assignment to the various jurisdictions is the same; because income, and hence income taxes, must economically, fiscally, and constitutionally be attributed to the jurisdictions in which it arises. And these are the same jurisdictions in which governmental services are rendered, because the same factors which entail governmental costs produce business income: property and people. Thus, by measuring relative quantities of property and people in various locations we determine, in addition to relative quantities of governmental services, relative quantities of production of income. Again, the location of a business's customers is irrelevant.

As pointed out above, the purpose and effect of a "destination sales factor" is to subsidize exports and impose a tariff on imports. It does not "apportion" income, but merely identifies the income from that segment of the business which consists of manufacturing in one jurisdiction and selling to customers in another.

Even in its earliest developments, the sales factor didn't make much sense. The earliest business income taxes were apportioned on the basis of location of property. *Underwood Typewriter Company* v. *Chamberlain*, 254 U.S. 113 (1920); *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271 (1924); *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123 (1931); *Kent-Coffey Mfg. Co.* v. *Maxwell*, 291 U.S. 642 (1934). Except in the exceptional circumstances of *Hans Rees'*, acceptable results were achieved.

Later payroll was added as an additional consideration. It didn't greatly affect the result, because to a considerable extent property and payroll tend to locate together. Not entirely, however, as for example a labor-intensive branch of a manufacturing business may have considerable payroll but very little property. The addition of the payroll factor was therefore an improvement in the measurement of income-producing activity.

Massachusetts added a "sales" factor, initiating what was long called "the Massachusetts formula". It was a three-factor formula, equally weighted, of property, payroll and sales—*with sales assigned to the point of shipment.* Somewhat later, various jurisdictions began to attribute sales, not to the points of shipment, but to the locations of sales offices: "sales through offices". This, of course, greatly exaggerated the income-producing importance of those offices, since their property and payroll were already included in the apportionment numerators, but it at least attributed income to something done by the taxpayer.

Finally, and quite recently, we arrived at the attribution of sales to the location of the customer: "destination sales". This scheme was developed in industrial, high-tax states (such as Michigan) to subsidize exports into lower-tax states.

Whatever respectability, if any, may be attributed to the "destination sales factor" as a subsidy for exports is wiped out when the reverse of the coin is examined: a tariff on imports. That is its purpose and effect, unconstitutional, at least when not modified by other factors. It is the desire of Iowa to make it easy for Iowa producers to compete in foreign markets by relieving them of all income tax on such business; and to handicap foreign producers by making them pay tax on 100% of their income from Iowa business already heavily, and properly, taxed in other states.

In the first section of this argument, we pointed out that such a program imposes an unconstitutional burden on interstate commerce. It is unconstitutional for other reasons. Due process, as applied to questions of state taxation of income, requires that a state refrain from taxing substantial income-producing activities occurring outside the state. A state income tax may be levied only on that portion of a taxpayer's net income which arises from its activities within the taxing state. *Wallace* v. *Hines*, 253 U.S. 66, 70 (1920); *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123, 135 (1931). But the "Due Process Clause", although convenient and customarily relied upon by courts, including this one, is not needed for that purpose. It is a fundamental principle of federalism that the legal, including tax, jurisdiction of a state is confined to its geographical jurisdiction. *New York, Lake Erie & Western R.R. Co.* v. *Pennsylvania*, 153 U.S. 628 (1894). It is perfectly clear that, as the trial court found, Iowa's assessments take in income attributable to Illinois and not Iowa.

Long ago this Court recognized that "income is the product of capital or labor or both combined"—no mention of customers or their location. *Stratton's Independence,*

Ltd. v. *Howbert*, 231 U.S. 399 (1913); *Eisner* v. *Macomber*, 252 U.S. 189 (1920); and *General Motors, supra*:

> "The standard three-factor formula can be justified as a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates. By contrast, the geographic distribution of a corporation's sales is, by itself, of dubious significance in indicating the locus of either factor." 380 U.S. at 561.

On its face, the single sales factor formula violates the due process clause of the Fourteenth Amendment and a basic principle of federalism in that it attempts to tax *all* the income arising from sales of tangible personal property in Iowa even though the product is manufactured outside that state. This is a patently unconstitutional approach to taxation of multistate corporations because it is indisputable that production of a product contributes a substantial part of the profit arising when it is sold:

> ". . . the enterprise of a corporation which manufactures and sells its manufactured product is ordinarily a unitary business, and all the factors in that enterprise are essential to the realization of profits." *Hans Rees', supra*, 282 U.S. at 133.

There is no accounting recognition of income until a product is sold. But it is likewise true that no product can be sold unless it is produced. The sale merely informs us when income is realized, not what gave rise to it. By attempting to tax all the income, the single sales factor formula takes no cognizance of the contribution which the creation of the product outside the state makes to the realization of income.

Furthermore, while the State of Iowa does render services to Moorman's business in that state, it is likewise

beyond question that Illinois, in which the corporation manufactures the products which it sells to Iowa customers, also renders services to such manufacturing. The Iowa formula refuses to recognize this obvious fact and, in so doing, taxes Moorman on an excessive amount of its income, including income which belongs to Illinois, in violation of the due process clause.

The district court found as a *fact* that the income which Iowa taxed in its entirety was ". . . to a greatest degree attributable to Illinois plant and personnel inputs" (A. 76) and further found as a *fact* that the amount of income so assessed was out of all reasonable proportion to the business done in Iowa (A. 77).

The Supreme Court of Iowa made no direct response to the findings of the district court, but repeated the oft-quoted language from *Wisconsin* v. *J.C. Penney,* 311 U.S. 435 (1940):

> "The Constitution is not a formulary. It does not demand of states observance of rigid categories nor precision of technical phrasing in their exercise of the most basic power of government, that of taxation. For constitutional purposes the decisive issue turns on the operating incidence of a challenged tax. A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society. . . The simple, but controlling question is whether the state has given anything for which it can ask return."

The Iowa Court then went on to hold that the Iowa formula

> ". . . is fairly calculated to assign to Iowa only that portion of the taxpayer's net income reasonably attributable to the trade or business done in Iowa since the taxing power exerted by the statute bears fiscal relation to the protection, opportunities and benefits given by the state." (A. 130).

There probably is no other passage in Supreme Court reports that is so often misapplied as Justice Frankfurter's felicitous phrases. There was in that case no quarrel with the apportionment formula. The issue was whether the "privilege dividend tax" was an additional income tax, and hence constitutional, or a tax on the "privilege" of paying dividends, which could not constitutionally be applied to Penney since all matters connected with dividends occurred in New York. The Wisconsin Supreme Court had said the tax was not an income tax. Justice Frankfurter and four other justices held that it was an income tax, and the quoted language tells why "practical operation" prevails over "technical phrasing."[7] Four justices dissented on the ground it was not an income tax in practical operation. In that same opinion, Justice Frankfurter warned against relying on "Ambiguous intimations of general phrases in opinions torn from the significance of concrete circumstances. . ." The principal quotation was apt in the "concrete circumstances" of *Penney* but is meaningless in *Moorman.*

"The question" remains "simple", but it definitely is not "controlling" here. In the context of this case, in which the only issue is how much tax, not "whether", the Iowa court's language quoted above is an obvious non

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7. We wonder if much of the misuse of Justice Frankfurter's opinion could have been avoided had he said—as we think he clearly meant—"in *proportion* to opportunities" instead of "in relation to opportunities".

sequitur. It says the "apportionment" is fair merely because Moorman is taxable.

The district court recognized the distinction (A. 74):

> The more narrow question presented, however, acknowledging that ". . . the tax in practical operation has relation to opportunities benefits [and] protection conferred or afforded by [Iowa is whether] the tax is fairly apportioned to the commerce carried on within [this State]." *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission*, 390 U.S. 317, 325 (1968) (fn. 5).

The Supreme Court of Iowa then cited the following five decisions of this Court to support its finding: *Underwood Typewriter Co.* v. *Chamberlain*, 254 U.S. 113 (1920); *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271 (1924); *National Leather Co.* v. *Massachusetts*, 277 U.S. 413 (1928); *Kent-Coffey Mfg. Co.* v. *Maxwell*, 291 U.S. 642 (1934), *aff'g per curiam* 204 N.C. 365, 168 S.E. 397 (1933); *Ford Motor Co.* v. *Beauchamp*, 308 U.S. 331 (1939), on the theory that this Court had placed its imprimatur on *any* single factor method of apportionment. This is the same fundamental error in reasoning made by the Court of Appeals in *General Motors* v. *District of Columbia, supra* (see 336 F.2d at 897).

Moorman's position is that the five above-cited cases provide no support for the Iowa court's inference but, indeed, that the relevant ones disprove its hypothesis and support the trial court's decision.

The *Ford* case is irrelevant because it does not deal with a tax on or measured by net income but rather is an excise based on the value of the corporation's assets employed in the state, which is quite distinct from an income tax. That case involved the Texas franchise tax,

which is an excise on the corporate privilege of doing intra-state business. *National Leather* involved a similar Massachusetts tax. Such franchise taxes are fairly common and the State of Iowa imposes such a tax on both domestic and foreign corporations (§496A.126 and §496A.-127, Code of Iowa).

Of the remaining three cases, *Underwood, Kent-Coffey,* and *Bass* dealt with statutes imposing taxes on or measured by net income, wherein the apportionment formula was a single property factor. The types of apportionment formulae in those cases are, on their face, sound, in that they are reasonably proportionally related to the sources of the taxpayer's income and the social costs which it generates.

Since "income is the product of capital or labor or both combined", property (capital) in a jurisdiction is a reasonable measure of income produced there. That is wholly incompatible with destination sales (location of customers) standing alone since location of customers does not indicate location of either business activity or governmental services. In *Underwood,* the Court rejected the taxpayer's argument in effect for consideration of sales.

In 1965, this Court had occasion to review the validity of a formula identical to that contained in the Iowa statute. *General Motors Corporation* v. *District of Columbia, supra.*

In that case, the District of Columbia Income and Franchise Tax Act of 1947 provided that

> (t)he measure of the franchise tax shall be that portion of the net income of the corporation . . . as is fairly attributable to any trade or business carried on or engaged in within the District . . . . (380 U.S. at 554).

That act provided that the District Tax Commissioners were to prescribe regulations to determine the portion of income "fairly attributable" to the District. The District Tax Commissioners adopted the following regulation:

> Where income for any taxable year is derived from the manufacture and sale or purchase and sale of tangible personal property, the portion thereof to be apportioned to the District shall be such percentage of the total of such income as the District sales made during such taxable year bear to the total sales made everywhere during such taxable year. (380 U.S. at 555).

The Court of Appeals found that *only* a *single* division of G.M.'s *total* income was required. That is, by multiplying G.M.'s entire net income by the single sales factor, that portion taxable in the District of Columbia could be determined.

The appeals court rejected the taxpayer's argument that this so-called "apportionment" of G.M.'s income was not an apportionment at all, but merely determined the portion of the taxpayer's income derived from manufacture outside the District and sales in the District.

This Court repudiated the Court of Appeals reasoning by stating that an apportionment formula must "take account of the geographic spread of the major dimensions of a business" (380 U.S. at 558, fn. 8) and found that "The standard three-factor formula can be justified as a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates." With respect to the single sales factor method the Court said: "By contrast, the geographical distribution of a corporation's sales is, by itself, of dubious significance in indicating the locus of either factor." (380 U.S. at 561).

The Iowa court, while skirting the point so far as direct statement is concerned, falls into the same fallacy as did the Court of Appeals in *General Motors*: it assumes that because Moorman's income from business wholly unrelated to Iowa—e.g., goods manufactured in Texas and sold to Texas customers—is not taxed by Iowa, there has been an "apportionment" of Moorman's *entire* income and therefore no further apportionment is required.

What the Iowa court overlooks is that the "reasonably attributable" division of income can be achieved *either* by finding the amount of income related to "Iowa sales" and apportioning that amount, *or* by apportioning entire net income, *and under any true apportionment formula the result will be exactly the same.*

In Appendix E hereto, beginning at p. A6, we set forth a tabulation, using Moorman's actual figures, demonstrating conclusively why the theory—that excluding wholly unrelated business is "apportionment"—is completely invalid. To make the point, more simply, the following is a hypothetical example, assuming for illustration only that apportionment should be on the basis of a property ratio (as was approved by this Court in *Underwood Typewriter Co.* v. *Chamberlain*, 254 U.S. 113; *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271; and *Kent-Coffey Mfg. Co.* v. *Maxwell*, 291 U.S. 642):

Total sales (gross receipts)	$1,000,000
Total net income	100,000
Total property	1,000,000
Sales to Iowa Customers	100,000
Property in Iowa	10,000

Using the formula in the cited cases, and considering first apportioning entire net income:

Property ratio: $\frac{\$ \quad 10{,}000 \text{ Iowa}}{\$1{,}000{,}000 \text{ Total}} = 1\% \text{ Iowa}$

1% of $100,000 total income = $1,000

Considering next finding the total income from that segment of the business consisting of manufacturing and selling goods to Iowa customers:

Sales ratio: $\frac{\$ \ 100{,}000 \text{ Iowa}}{\$1{,}000{,}000 \text{ Total}} = 10\% \text{ Iowa}$

10% of $100,000 total income = $10,000 segment income

This is the *total* income from the segment of its business which results in sales to Iowa customers.

The sales ratio determines also the total property used to produce the goods in that segment:

10% of $1,000,000 total property = $100,000 segment property

Property ratio: $\frac{\$ \ 10{,}000 \text{ Iowa}}{\$100{,}000 \text{ Total segment}} = 10\% \text{ Iowa}$

10% of $10,000 segment income = $1,000

The above demonstration and especially the actual figures in the tabulation in Appendix E hereto, show why it is that the sales factor "apportions" nothing but merely identifies the income subject to apportionment—the income derived from the entire business of manufacturing without and selling into the taxing jurisdiction.

In *General Motors*, for the first time, this Court was faced with an apportionment formula that clearly was irrational. It responded to that situation by the use of, among other things, a hypothetical fact situation[8] to demonstrate the obvious—the single destination sales factor formula attributes to the taxing jurisdiction an excessive amount—100%—of the taxpayer's income in relation to the sources of income within the jurisdiction and the services rendered by that jurisdiction. This, very simply, is why that appeal and this one are not defeated, but rather buttressed, by the judicial approval of formulae applied in prior cases involving the single property factor and the three-factor formulae.

Based on the stipulation, the trial court found that for the fiscal year ending in 1968 the percentage of Moorman's payroll associated with its Illinois operations was 41% of its payroll everywhere; the Iowa payroll percentage was 15.63%. Of its property everywhere, that located in Illinois represented 84.29%, while that in Iowa was a mere 5.27%. Finally its sales in Iowa for that year were 21.88% of its sales everywhere (A. 76).

The trial court then observed (A. 76):

> "Yet in light of Moorman's relatively small property holdings and payroll contributions in Iowa (none of which are attributable to the manufacture of goods sold here), this State taxes 100 percent of in-state sales (21.88% of income for 1968), which are to a great degree attributable to Illinois plant and personnel inputs."

---

8. 380 U.S. 553, 557. A corporation manufacturing entirely in Maryland and selling entirely in the District would have its entire income taxed in the District.

Moorman maintains that the foregoing irrefutably demonstrates that the effect of the Iowa formula is to tax income-producing activities occurring in Illinois in violation of the Due Process Clause of the Fourteenth Amendment and a fundamental principle of federalism.

Furthermore, it is undisputed that while the State of Iowa renders services to Moorman, it obviously does not render *all* the services which benefit Moorman's business of manufacturing in Illinois and selling in Iowa, and thus is not entitled to tax all the income arising from Moorman's sales in Iowa. The Iowa formula clearly fails to allow a reasonable apportionment of income associated with Iowa sales to be attributed to Illinois, which also provides benefits to Moorman with respect to such income. This failing of the Iowa formula to apportion tax in relation to benefits given clearly deprives Moorman of its property without due process of law.

The Iowa Supreme Court rejected the evidence of extra-territorial taxation set forth above as failing to be sufficient in either quantum or quality to satisfy the burden of proof imposed upon Moorman.

The Iowa statute, in prescribing a fraction the numerator of which is sales to Iowa customers and the denominator of which is sales everywhere, and applying that fraction to total net income rests on the assumption that every dollar of gross receipts (sales) relates to the same amount of net income as every other dollar of gross receipts. That assumption is, for this purpose, both economically and legally sound

That assumption necessarily includes the corollary assumption that costs (deductions) are similarly distributed —if they were not, the profit would vary from sale to sale. Thus, every dollar's worth of property makes the

same contribution to net income as every other dollar's worth of property and every dollar of payroll makes the same contribution to net income as every other dollar of payroll.

The figures establishing all three ratios are stipulated (A. 54). Therefore, the ability to calculate income attributable to Iowa is well-established by applying the assumptions to the stipulated figures in conformance with practice as to assumptions accepted by this Court in *Underwood; Bass, Ratcliff & Gretton; General Motors; all supra. Butler Bros.* v. *McColgan*, 315 U.S. 501 (1942), and others.

The Iowa court seems to say that Moorman has not proved its case because it has not used separate accounting to establish its Iowa income. That method was held impermissible in the case of a unitary business and the foregoing assumptions were applied instead. *Butler Bros., supra.*

This Court has in the past declined to prescribe any specific formula for division of income. No such demand is made in this case, since the parties have stipulated that if the single-sales-factor is invalidated, they will apply the standard three-factor formula.

We do not want to be understood to urge proscription of the "destination sales" factor in a three-factor formula. To do so would be unreasonable. Clearly it could on constitutional grounds, be stopped as a penalty on imports. The result would be that taxpayers, such as Moorman, would have some of their income escaping tax altogether —a socially undesirable result. Moorman accepts the philosophy of this Court in *General Motors*: That the three-factor method is a "rough, practical" method of apportionment.

Finally, the Iowa court rejects this Court's reasoning in *General Motors* as having no bearing on this case for two reasons:

(1) That decision was statutory only, and

(2) The District of Columbia statute requiring that net income derived from a trade or business within and without the District shall "be deemed to be income from sources within and without the District" has "no analogue in the Iowa statute and can scarcely be found in the due process clause" (A. 130).

Moorman acknowledges that the *General Motors* decision of this Court was a statutory interpretation. Nevertheless, the statements of this Court outlining the inherent invalidity of a method of "apportionment" based on sales alone were a reiteration of constitutional principles of long standing. If *General Motors* truly was intended to reach "beyond the shores of the Potomac", the Iowa Court's view of that case is patently in error.

III. The Single "Destination Sales" Factor Denies Equal Protection.

The three major points: unconstitutional burden on interstate commerce; unconstitutional denial of due process, and unconstitutional violation of a basic principle of federalism—are sufficient. Nevertheless, we draw the Court's attention to the denial of equal protection which is inherent in Iowa's single "destination sales formula", particularly in relation to Illinois' (proper) three-factor formula. As this Court said in *General Motors,* after noting the double-taxation upon shipments *into* the District of Columbia:

"Conversely, in some cases enterprises will have their payroll and plant located in sales-factor jurisdictions and make their sales in three-factor jurisdictions so

that only 33% of their incomes will be subject to state taxation." (380 U.S. at 560).

That is what happens here: while Moorman is double-taxed on its income from sales to Iowa customers, its Iowa competitors are taxed on only one-third of their income from Illinois customers.

The denial of equal protection of the laws inherent in the Iowa formula can be readily demonstrated by a comparison of two hypothetical situations:

Situation 1: Corporation A manufactures all its products within the State of Iowa, but sells all of its products outside the State of Iowa.

Situation 2: Corporation B manufactures all of its products outside the State of Iowa, but sells all of its products within the State of Iowa.

Under the Iowa formula, the following pattern of taxation prevails:

Situation 1: None of the net income of Corporation A is taxable by the State of Iowa. This result is blatantly unfair. All of the property and people involved in manufacturing the product are located in Iowa, with only sales activity occurring outside the state. Yet despite the concentration of economic activity and the substantial rendition of services by the State of Iowa, Iowa collects no tax on A's income.

Situation 2: All of the net income of Corporation B is taxable by the State of Iowa. This result is as unreasonable as that in Situation 1. All of the productive factors of Corporation B are located outside Iowa and another state renders substantial services to B and its employees.

The foregoing hypothetical examples teach an unmistakable lesson: The Iowa formula penalizes out-of-state manufacturers and subsidizes Iowa-based firms which sell the bulk of their products outside the state.

It may appear to a casual observer that Section 422.33 (1), Code of Iowa, does operate uniformly upon all corporations engaged in the manufacture or sale of tangible personal property in the State of Iowa—the net income of all such corporations is "apportioned" to the state in the ratio that their sales in Iowa bears to their total sales. The above demonstration goes beyond appearances into the practical imposition of very different burdens on taxpayers whose situations should be treated equally. In the examination of a taxing statute, we must heed the warning of Mr. Justice Rutledge in *Nippert* v. *City of Richmond*, 327 U.S. 416, 431 (1946), in discussing one of the famous "drummer" statutes:

> "It is no answer, as appellee contends, that the tax is neither prohibitive nor discriminatory on the face of the ordinance; or that it applies to all local distributors doing business as appellant has done. Not the tax in a vacuum of words, but its practical consequences for the doing of interstate commerce in applications to concrete facts are our concern. To ignore the variations in effect which follow from the application of the tax, uniform on the face of the ordinance, to highly different fact situations is only to ignore those practical consequences. In that blindness lies the vice of the tax and of appellee's position."

The trial court found that Moorman's Commerce Clause and Due Process rights had been violated, but not its Equal Protection rights. That conclusion was based on a misunderstanding of Moorman's position: the court

justified a tax on "corporations" as a class distinct from other taxpayers. We agree, but our argument was that some members of the properly delineated class (corporations) may not be discriminated against as compared to other members of the same class. The Iowa legislature has created a valid classification of "corporations" which Section 422.33 purports to treat throughout in like manner, without discrimination as to location. But, as shown above, this purported equal treatment is illusory.

The trial court's reasoning, adopted by the Supreme Court of Iowa, is devoted to discussion of classification, citing *Lehnhausen* v. *Lake Shore Auto Parts Co.*, 410 U.S. 356 (1973) for the proposition that corporations may be taxed differently from individuals. There is no such issue.

IV. Application of the Single "Destination Sales" Factor to Moorman Is Unconstitutional.

Earlier portions of this brief have dealt with the issue of whether the single sales factor method of assigning corporate income to Iowa contained in Section 422.33(1)(b), Code of Iowa, is unconstitutional on its face under the due process, commerce clause and equal protection provisions of the Constitution and tramples on an important principle of federalism.

In finding that this formula is unconstitutional on its face under the due process and commerce clauses, the trial court did not feel it had to consider whether such method was unconstitutional in its *application* to Moorman. That Court merely analyzed the Moorman figures to substantiate that the hypothesis of this Court in *General Motors* v. *District of Columbia, supra*, was correct—multiple taxation does occur under the Iowa system of taxation.

The Supreme Court of Iowa, however, reversed the trial court's holding that the Iowa formula was unconstitu-

tional on its face. As to the issue of its constitutionality as applied to Moorman, the court found that Moorman had failed to carry its burden of proof because it had not proved that it is "dissimilar from the typical unitary business organization." (A. 139). Moorman had not sought any such distinction and, in fact, claims to be "a typical unitary business organization."

A determination of the constitutionality of the Iowa method as it applies to Moorman necessitates an analysis of Moorman's particular situation. The parties stipulated a substantial amount of statistical information concerning Moorman during the years at issue. This information has been analyzed in earlier portions of this brief in great detail. These data demonstrate beyond question that the State of Iowa is taxing income partially created in Illinois, is causing actual, substantial multiple taxation to be visited upon Moorman and is placing a burden upon Moorman's interstate activities, as the trial court found.

Nowhere in its opinion does the Iowa court refute these unassailable conclusions derived from the stipulated statistical data. Yet the Iowa court finds that Moorman has failed in meeting its burden of proof in this area. Moorman asserts (and the Iowa court agreed) that by reason of the very nature of a unitary business it is impossible to assign each item of income and expense on a state-by-state basis. Indeed, the Iowa statute requires only that *net* income be apportioned. Moorman has placed in evidence via the stipulation sufficient relevant information to demonstrate the presence of the evils arising for the Iowa apportionment formula catalogued above.

It is submitted that if there is indeed *any* type or quantum of evidence sufficient to carry a taxpayer's burden of proof in this type of case, Moorman has more than fulfilled the requirements. As noted in the Iowa

court's decision (A. 119), the state must come forward with evidence to counter that provided by Moorman. This the state has failed to do.

Whether Moorman is in a situation similar or dissimilar to other corporations is immaterial when the issue is constitutionality in *application*, for all that need be shown is that the State of Iowa is levying a tax on a greater portion of Moorman's net income arising from Iowa sales than is permissible under the federal Constitution.

V. Affirmance of the Iowa Decision Would Be a Serious Detriment to the American Common Market.

> "In any case, the sheer inconsistency of the District formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and an uneconomic pattern of plant location . . ."—*General Motors, supra* at 560.

There is a strong incentive for each state, acting by itself, to violate the basic concept of federalism—the common market—to its own shortsighted benefit. Thus, and not unnaturally, the Supreme Court of Iowa gave far greater consideration to the briefs extolling Iowa's destination sales formula than it did to either Moorman's logical exposition of the law or the splendid analysis by the trial judge.

As the fifteen economists (William J. Baumol, *et al.*), said in their brief *amicus curiae* urging the Court to accept this appeal:

> "One of the most important ways in which competition controls economic activity is to create pressures to eliminate higher cost producers. When these higher costs are due to inefficient management or inefficient production techniques, this pressure to eliminate cer-

tain firms or force them to perform more efficiently is unequivocally socially desirable. However, competition will have this excluding effect regardless of the particular cause of higher costs. Thus the effects of a differentially higher tax rate will be precisely the same on a firm in a competitive industry as will a poor management policy that 'costs' the same amount. But in the tax case competition is actually prevented from performing the socially useful function of eliminating undesirable economic inefficiencies. And this is exactly the effect of the Iowa 'single factor' tax formula when adopted in the face of the otherwise universal use of a three-factor attribution test." (Page 2 of their brief).

Note how well that economic exposition explains the basis for our Equal Protection argument, and how strongly it supports what this Court said in *General Motors*, quoted at p. 37 *supra*.

As previously stated, the purpose and effect of the "destination sales" factor is to subsidize exports and impose a tariff on imports. If it is given only one-third weight it can be tolerated in the context of the almost universal use of the equally weighted three-factor formula. But if Iowa can succeed in its present effort, other jurisdictions will surely follow—selfish and shortsighted pressures from local businesses will be irresistible. Again quoting the economists *amici*:

> "As political pressures build in one state and then another to secure these hidden competitive benefits for domestic businesses through selection of appropriate tax formulas, the spector of a severely damaging, yet not openly declared trade war between states begins to threaten. No conceivable economic advantage

> could justify the economic costs attendant upon such conflict." (Page 7 of their brief).

Perhaps discouraged by this Court's decision in *General Motors, supra*, no state but Iowa has attempted the gross discrimination against interstate commerce which is inherent in the single "destination sales" factor. Several others are, however, inching up on it through double-weighting the sales factor: Florida, 1971; Wisconsin, 1975; New York, 1976; Massachusetts, 1977. Is there any doubt they will move from double-weight to 100% weight if Iowa can do it?

States and communities tend to welcome industrial establishments, partly to create jobs and even more to acquire tax base. Many of them put on elaborate promotions, and some offer special inducements: Using the local government's ability to offer tax-free interest to bond buyers; property tax exemptions for limited periods. The Iowa device of handicapping out-of-state producers while bonusing local business is an inducement to "an uneconomic pattern of plant location".

Again quoting the economists:

> "Thus the Iowa tax based on sales revenue for an Illinois corporation producing in Illinois in effect becomes a tax on property and payrolls in Illinois. But these items are already taxed in Illinois via the three-factor formula. . . Regardless of the intention of the framers of the Iowa tax the effect is clearly contrary to the principle of federalism that underlies the Commerce Clause of the United States Constitution. The necessary effect of this tax is precisely the same as an Iowa tariff imposed on Illinois or other corporations doing business in Iowa in competition with Iowa companies. To allow this state of affairs to persist in any

state is to invite, indeed even to force, retaliation by other states. . . It is of utmost importance that this Court address itself once again to this issue and prevent the development of debilitating internal conflict in the United States." (Page 7 of their brief).

Boston Stock Exchange v. *State Tax Commission, supra*:

". . . the fundamental purpose of the [Commerce] Clause is to assure that there be free trade among the several States."

CONCLUSION

As we said in our Jurisdictional Statement, and has been emphasized by the briefs *amicus curiae*, such taxpayer representatives as the Motor Vehicle Manufacturers Association and the Council of State Chambers of Commerce, the broad spectrum of academic economists, and even the Multistate Tax Commission, the organized state tax administrators (they didn't say it just that way): the decision of this Court is needed to halt the effort of Iowa to shift its tax burden to foreigners and remove the temptation for other states to do likewise.

The Iowa single "destination sales" formula is so incompatible with the three-factor formula used by Illinois and most other states that it cannot be allowed to survive.

It unduly burdens interstate commerce by imposing double taxation.

It violates due process and, even more importantly, the fundamentals of federalism, by taxing values not within its jurisdiction.

It denies equal protection by giving advantages to domestic producers which it denies to foreign producers.

Its survival would seriously disrupt our United States common market.

For the reasons stated, it is submitted that the decision of the Supreme Court of Iowa should be reversed and the single sales factor for division of income for tax purposes in the Iowa statute be declared unconstitutional.

Respectfully submitted,

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APPENDIX

APPENDIX A

CONSTITUTION OF THE UNITED STATES

ARTICLE I.

* * *

Section 8. The Congress shall have Power. . .

* * *

To regulate Commerce . . . among the several States. . .;

AMENDMENT 14.

Section 1. * * *; nor shall any State deprive any person of . . . property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

APPENDIX B

CODE OF IOWA

422.33 Corporate tax imposed

A tax is hereby imposed upon each corporation organized under the laws of this state, and upon every foreign corporation doing business in this state, annually in an amount equivalent to four percent of the net income received by such corporation during the income year.

1. If the trade or business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income, but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on the portion of the net

income reasonably attributable to the trade or business within the state, said net income attributable to the state to be determined as follows:

a. Interest, dividends, rents and royalties (less related expenses) received in connection with business in the state shall be allocated to the state, and where received in connection with business outside the state, shall be allocated outside of the state.

b. Net income of the above class having been separately allocated and deducted as above provided, the remainder of the net income of the taxpayer shall be allocated and apportioned as follows:

* * *

Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

The gross sales of the corporation within the state shall be taken to be the gross sales from goods sold and delivered within the state, excluding deliveries for transportation out of the state.

For the purpose of this section, the word "sale" shall include exchange, and the word "manufacture" shall include the extraction and recovery of natural resources and all processes of fabricating and curing. The words "tangible personal property" shall be taken to mean corporeal personal property, such as machinery, tools, implements, goods, wares, and merchandise, and shall not be taken to mean money deposits in banks, shares of stock, bonds, notes, credits, or evidence of an interest in property and evidences of debt.

2. If any taxpayer believes that the method of allocation and apportionment hereinbefore prescribed, as administered by the commission and applied to his business, has operated or will so operate as to subject him to taxation on a greater portion of his net income than is reasonably attributable to business or sources within the state, he shall be entitled to file with the commission a statement of his objections and of such alternative method of allocation and apportionment as he believes to be proper under the circumstances with such detail and proof and within such time as the commission may reasonably prescribe; and if the commission shall conclude that the method of allocation and apportionment theretofore employed is in fact inapplicable and inequitable, it shall redetermine the taxable income by such other method of allocation and apportionment as seems best calculated to assign to the state for taxation the portion of the income reasonably attributable to business and sources within the state, not exceeding, however, the amount which would be arrived at by application of the statutory rules for apportionment.

(Note: The foregoing Section 422.33, Code of Iowa, is as it appears at Vol. II, p. 1669 of the 1966 edition of the Code; it has been amended subsequently in respects not material to this case and appears in its latest form in Code of Iowa (1977), Vol. II, p. 2078.)

422.35 Net income of corporation—how computed.

The term "net income" means the taxable income less the net operating loss deduction, both as properly computed for federal income tax purposes under the Internal Revenue Code of 1954, with the following adjustments:

1. Subtract interest and dividends from federal securities.

2. Add interest and dividends from foreign securities and from securities of state and other political subdivisions exempt from federal income tax under the Internal Revenue Code of 1954.

3. Where the net income includes capital gains or losses, or gains or losses from property other than capital assets, and such gains or losses have been determined by using a basis established prior to January 1, 1934, an adjustment may be made, under rules and regulations prescribed by the state tax commission, to reflect the difference resulting from the use of a basis of cost or January 1, 1934, fair market value, less depreciation allowed or allowable, whichever is higher. Provided that the basis shall be fair market value as of January 1, 1955, less depreciation allowed or allowable in the case of property acquired prior to that date if use of a prior basis is declared to be invalid.

4. Subtract federal income taxes paid or accrued, as the case may be, during the tax year, adjusted by any federal income tax refunds; and add the Iowa income tax deducted in computing said taxable income.

5. Add the amount by which the basis of qualified depreciable property is required to be increased for depreciation purposes under the Internal Revenue Code Amendments Act of 1964 to the extent that such amount equals the net amount of the special deduction allowed on the basis of the amount by which the depreciable basis of such qualified property was required to be reduced for depreciation purposes under the Internal Revenue Code Amendments Act of 1962. The "net amount of the special deduction" shall be computed by taking the sum of the amounts by which the basis of qualified property was required to be decreased for depreciation purposes for the years 1962 and 1963 and subtracting from it the sum

of the amounts by which the basis of such property was required to be increased, prior to 1964, for depreciation or disposition purposes under the Internal Revenue Code Amendments Act of 1962.

Provided, however, that a corporation affected by the allocation provisions of section 422.33 shall be permitted to deduct only such portion of the deductions for net operating loss and federal income taxes as is fairly and equitably allocable to Iowa, under rules and regulations prescribed by the state tax commission.

(Note: The foregoing Section 422.35, Code of Iowa, is as it appears at Vol. II, p. 1670 of the 1966 edition of the Code; with respect to taxable years beginning on or after January 1, 1967, Subsection 4 was amended by inserting "fifty (50) per cent of the" preceding the words "federal income taxes", Acts of 1967 (62 G.A.) ch. 348, §17. The latest form of Section 422.35 appears in Code of Iowa (1977), Vol. II, p. 2080.)

APPENDIX C

The Illinois Income Tax Act, 120 Ill. Rev. Stat. §3-304 provides as follows:

§3-304. Business income of persons other than residents

(a) In general. The business income of a person other than a resident shall be allocated to this State if such person's business income is derived solely from this State. If a person other than a resident derives business income from this State and one or more other states, then, except as otherwise provided by this Section, such person's business income shall be appor-

tioned to this State by multiplying the income by a fraction, the numerator of which is the sum of the property factor (if any), the payroll factor (if any) and the sales factor (if any), and the denominator of which is 3 reduced by the number of factors which have a denominator of zero. * * *

APPENDIX D

The Uniform Division of Income for Tax Purposes Act provides as follows:

§3. For purposes of allocation and apportionment of income under this Act, a taxpayer is taxable in another state if (1) in that state he is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporate stock tax, or (2) that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not.

§9. All business income shall be apportioned to this state by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three.

APPENDIX E

COMPARATIVE COMPUTATION OF APPORTIONMENT

Usual computation of net income, and the computations of Moorman's tax returns under the apportionment formula which it used, are shorthand computations which produce accurate results but which tend to obscure what is being

done. Working them in longhand helps to clarify. The Iowa statute starts the computation of taxable income with federal taxable income, which is determined by subtracting from gross receipts the expenses and other deductions attributable thereto, with certain adjustments. (Code of Iowa, Chapter 422). We know the amounts of total gross receipts and the part thereof derived from sales to Iowa customers. Applying that ratio to the known total expenses and other deductions, we determine the deductions allocable to Iowa receipts. Thus, for 1968 (figures for convenience are in thousands of dollars and rounded):

	Longhand Method	Shorthand Method
(a) Iowa Receipts	21,380	21,380
(b) Total Receipts	97,720	97,720
(c) Total Deductions	90,643	
(d) Total Income		7,077
(e) Segment Deduction (a÷b) X c	19,832	
(f) Segment Income a – e	1,548	
(g) Segment Income (a÷b) x d		1,548

Either method arrives at the same amount of net income derived from the segment of the business carried on both within and without Iowa. That is the amount which is to be apportioned. Again, the apportionment can be done either longhand (for clarity) or shorthand (for convenience).

Here we illustrate both, again with 1968 figures, on the principle enumerated by this Court, that "payroll"

and "property" fractions are sound measures of relative business activity:

		Longhand Method	Shorthand Method
(a)	Iowa Receipts	21,380	
(b)	Total Receipts	97,729	
(d)	Total Income		7,077
(f)	Segment Income	1,548	
(h)	Iowa Payroll	3,739	3,739
(i)	Total Payroll	23,919	23,919
(j)	Segment Payroll (a÷b) X i	5,233	
(k)	Iowa Property	1,133	1,133
(l)	Total Property	21,501	21,501
(m)	Segment Property (a÷b) X l	4,704	
(n)	Iowa Income $\frac{(h\div j) + (k\div m) \text{ X } f}{2}$	739	
(o)	Iowa Income $\frac{(h\div i) + (k\div l) \text{ X } d}{2}$		739

Longhand or shorthand, the result is the same; but the longhand method shows more clearly the illogic of using a sales factor, either alone or in conjunction with other factors, for "apportionment" purposes. When the ratio of gross receipts has been applied to determine the amount of net income attributable to the selected segment, it has exhausted its function and cannot validly be used

again to divide up that income. Nevertheless, there are practical reasons for a three-factor formula, including sales, as this Court noted in *General Motors*. That feature can be added to the tabulation as follows:

		Longhand Method	Shorthand Method
(p)	Iowa Income $\frac{(\ (h\div j) + (k\div m) \text{ X } f)+f}{3}$	$1,008	
(q)	Iowa Income $\frac{(h\div i) + (k\div l) + (a\div b) \text{ X } d}{3}$		$1,008

The longhand method clearly reveals the duplication in the treatment of income; that is, using the income—f—to apportion itself. The effect is arbitrarily to assign or allocate one-third of the apportionable income to Iowa and then to apportion the remaining two-thirds. The identical principle is involved in, and the identical result achieved by, the shorthand method. This last is the one used in Moorman's returns, and which has been stipulated to be the method to be used if this Court finds the single destination sales factor constitutionally unacceptable. (The above figures are based on the Director's findings of segment income, etc. and differ from those in the return —but the method is identical.)

Supreme Court, U. S.
FILED
JAN 25 1978
MICHAEL RODAK, JR., CLERK

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1977

NO. 77-454

MOORMAN MANUFACTURING COMPANY

Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE
STATE OF IOWA,

Appellee.

On Appeal From The Supreme Court
Of The State of Iowa

BRIEF FOR THE APPELLEE

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IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1977

NO. 77-454

MOORMAN MANUFACTURING COMPANY,

Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE
STATE OF IOWA,

Appellee

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

BRIEF FOR APPELLEE

OPINIONS BELOW

The Findings of Fact and Conclusions of Law of the Polk County District Court, Equity No. CE 3-1595, filed December 17, 1976, that Court's Ruling on Joint Motion to Reconsider and Supplemental Findings, and that Court's Judgment and Decree are unreported (A. 56). The decision of the Iowa Supreme Court, entered May 25, 1977, is reported at 254 N.W.2d 737 (Iowa 1977). That opinion and the unreported order denying rehearing entered June 27, 1977 are in the Appendix (A. 103,157).

JURISDICTION

Moorman invokes the jurisdiction of this court under 28 U.S.C. § 1257(2) since the Iowa Supreme Court held that the Iowa net income tax apportionment formula contained in § 422.33(1)(b), Code of Iowa, 1975, for reasonably attributing to Iowa a portion of Moorman's net income derived from the manufacture or sale of tangible personal property by the ratio which gross sales made within Iowa bear to total gross sales, did not, on its face or as applied to Moorman's net income, violate the commerce clause and the due process and equal protection clauses of the fourteenth amendment to the United States Constitution. The jurisdictional statement was filed September 22, 1977 and the Motion to Dismiss was filed October 20, 1977. Probable jurisdiction was noted November 14, 1977, 46 U.S.L. Week 3317 (U.S. Nov. 14, 1977), to review this decision of the Iowa Supreme Court.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Art. I, Sec. 8, Cl. 3 of the Constitution of the United States and the Due Process and Equal Protection Clauses of the Fourteenth Amendment thereto are set forth in Appendix A,p.Al, infra.

The relevant sections of the Code of Iowa, being Sections 422.33 and 422.35, Code of Iowa, 1975, contained in Volume II pages 1924 and 1925, are set forth verbatim in Appendix B, pp.A1-A4.

QUESTIONS PRESENTED

Whether the single-factor destination sales formula for the apportionment of net income prescribed by the Iowa income tax statute:

(1) discriminates against interstate commerce through the device of multiple taxation;

(2) subjects to Iowa tax a corporation's income out of all reasonable proportion to the business transacted in Iowa;

(3) constitutes the extraterritorial taxation of income; and

(4) subsidizes exports and imposes a tariff on imports;

in violation of the Commerce clause and the Fourteenth Amendment's Due Process and Equal Protection clauses of the United States Constitution.

STATEMENT OF THE CASE

This case was presented to the Courts below upon a stipulation of facts (A. 20-55). The only question on appeal to this Court concerns the constitutionality of the Iowa single sales factor net income apportionment formula.

Moorman, an Illinois Corporation, was engaged, during its fiscal tax years in question, March 31, 1968 through March 31, 1972, in the business of manufacture and sale of animal feeds. Such feeds were manufactured by Moorman in five plants located in Texas, Nebraska, and Illinois and sold by Moorman salesmen in more than 30 states. During the aforementioned fiscal years, Moorman carried on substantial income producing activities in the state of Iowa. After sales of feeds were negotiated by Moorman's Iowa sales force of over 500 employees, delivery to Iowa customers was typically made from one of six warehouses operated by Moorman in Iowa. Moorman engaged in no manufacturing in Iowa and the products sold to Iowa customers were all manufactured in Illinois. For the years in question, Moorman filed Iowa income tax returns, apportioning income to Iowa upon the basis of a three factor formula,

consisting of sales, property, and payroll factors, computed by it. For the years in question, the Iowa Director of Revenue (Director) recomputed Moorman's Iowa apportionable net income by application of the Iowa sales factor formula, rather than the three factor formula computed by Moorman. After notice and opportunity for hearing, the tax assessments which are the subject of this appeal were confirmed by the Director (A. 2-8). Moorman appealed the Director's determination to the Polk County District Court. The constitutional issues presented to the District Court were stipulated (A. 29-31).

The District Court held that the Iowa sales formula, on its face, violated the Commerce and Due Process, but not Equal Protection, clauses of the United States Constitution (A. 88). In reaching these conclusions, the District Court stated that "no evidence beyond that in the stipulation was presented or is considered" (A. 57). The only evidence in the stipulation upon which the District Court predicated its factual findings causing it to conclude that the Iowa formula was facially unconstitutional consisted of a showing that a three factor formula as computed by Moorman would result in a lower percentage of net income apportionable to Iowa than would the Iowa single sales factor (A. 75-76, 83-84). This evidence, together with the District Court's unfounded assumption that Iowa taxed 100% of Moorman's net income from Iowa sales, caused the Court to conclude that, based upon the interplay of the Iowa and Illinois apportionment formulae only, the percentage of Moorman's 1968 net income actually taxed was 141.76% and similar conclusions were reached for the other tax years (A. 84). The District Court was of the view that the constitutionality of the Iowa apportionment formula could be analyzed solely in terms of abstract computations of a three factor formula and Iowa single factor formula (A. 75-76, 83-84). The District Court assumed that an apportionment formula is facially unconstitutional if it does not provide for geographical distribution of labor and capital, thus reading into the Constitution a preference for an equally weighted three factor property-sales-payroll formula to the exclusion of other formulae (A. 75-77). The nature of Moorman's unitary income producing activities in all states, the profitability of its operations in all states, the precise jurisdictional sources of Moorman's net income in all states, and Moorman's net income tax base computations in all states were simply never considered by the District Court in making its findings and conclusions. Prior constitutional apportionment precedents, with their appropriate constitutional principles, were deemed insignificant by the District Court (A. 85). The District Court based its facial unconstitutionality holding upon *General Motors Corporation v. District of Columbia*, 380 U.S. 553 (1965), despite the fact this Court expressly noted that such case was not decided on constitutional grounds (A. 77,85).

An additional Commerce Clause violation was found by the District Court based upon a hypothetical situation which assumed that the interplay between the Iowa and Illinois apportionment formulae gave the Iowa-based manufacturer a commercial advantage (A. 86). Such a finding was inconsistent with the District Court's initial statement to only consider the evidence in the stipulation (A. 57). As noted, infra, hypotheticals form no grounds for resolution of constitutional questions. Moreover, the conclusion here was inconsistent with the District Court's own determination that the equality of treatment of Iowa and non-Iowa corporations explained why the Iowa tax law was not in violation of the Equal Protection clause. (A. 72).

The Director appealed the District Court's decision to the Iowa Supreme Court, and Moorman cross-appealed. The Iowa Supreme Court unanimously reversed the District Court and held that the Iowa formula was facially constitutional and, further, that the formula was constitutional as applied to Moorman (A. 103-141). Unlike the District Court, the Iowa

Supreme Court noted that, for Due Process analysis, this Court's constitutional apportionment decisions recognize: (1) impossibility of achieving precise apportionment; (2) rough approximation is sufficient; (3) taxpayer's heavy burden in challenging apportionment formulae on constitutional grounds; and (4) the states are unrestricted in choosing apportionment formulae and have great leeway in making such choices (A. 130). The Iowa Supreme Court noted that for the Iowa formula to be facially unconstitutional, it must fail to achieve constitutional standards "in every conceivable situation," but that this could not logically happen (A. 131). The Court distinguished *General Motors Corporation v. District of Columbia*, supra, as expressly decided on nonconstitutional grounds, thus offering no precedent or support for facial invalidity of the Iowa sales formula (A. 125-130). The Court noted that Moorman's evidence merely showed a larger percentage of total net income apportioned to Iowa by the Iowa single factor formula than by Moorman's computed three factor formula, but that such evidence formed no basis to infer "either double taxation or a taxation of extraterritorial values" in violation of Due Process (A. 131-132).

The Due Process analysis along with the "potentially large deductions" in computation of the Iowa tax base were advanced as reasons by the Court for concluding that the Iowa formula did not facially violate the Commerce clause, the Court stating: "Clearly, a corporation in Moorman's situation is not taxed by Iowa on 100% of its income from Iowa sales" (A. 134). In essence, the Iowa Supreme Court concluded that the so-called "findings of fact" of the District Court were unjustified inferences, unsupported by the evidence, and were based upon unproven assumptions and improper analysis of the constitutional principles involved (A. 132,134).

The Iowa Supreme Court also determined that the Iowa sales formula did not facially violate Equal Protection, pointing

out that no evidence was introduced on this issue by Moorman which only attempted to show "extreme" hypothetical situations (A. 137). Thus, it was not shown, for Equal Protection purposes, that the Iowa sales formula subsidizes exports and imposes a tariff on imports.

The Court determined that the tenor of Moorman's contentions that the Iowa sales formula was unconstitutionally applied to its net income, as ordered by the Director, was inseparable from its allegations as to facial constitutionality (A. 138). Thus, having concluded the Iowa formula was facially valid, the Court held that Moorman had not carried its burden of showing that the Iowa formula was unconstitutionally applied to it (A. 138-139).

SUMMARY OF ARGUMENT

1. Prior constitutional precedents of this Court support the facial due process constitutionality of the Iowa statutory single sales factor net income apportionment formula. No showing has been made in this case that this presumptively valid formula produces, inherently, extraterritorial taxation or an income apportionment out of all reasonable proportion to corporate business transacted in Iowa. No such showing can be made by hypotheticals and assumptions as to the amount of income from Iowa sales taxed by Iowa.

2. The premise that the Iowa single sales factor formula operates to tax 100% of income derived from Iowa sales is unproven and false. Since this premise cannot be accepted, no showing was made that the Iowa sales formula facially causes multiple taxation and discriminates against interstate commerce in violation of the commerce clause. The abstract and hpothetical interplay of the Iowa formula and Illinois three factor formula is insufficient to demonstrate that the purpose and effect of the Iowa sales factor is to subsidize exports and

impose a tariff on imports. Moreover, precision in taxation is not required and if a formula produces rough approximation, it does not discriminate against interstate commerce.

3. All corporations doing business in Iowa and subject to Iowa income taxes are facially treated alike by the Iowa income tax scheme. Extreme hypotheticals are not proper tactics to demonstrate the facial invalidity of an apportionment formula under equal protection.

4. The tenor of Moorman's contentions as to facial constitutionality of the Iowa sales formula cannot be separated from its argument that the formula is invalid as applied to Moorman's net income. Nor was such a sufficient showing of invalidity presented. Therefore the Iowa formula is valid as applied to Moorman's net income.

5. Reversal of the decision of the Iowa Supreme Court would make the Constitution a formulary and inhibit the States, unduly, in the exercise of their fundamental power of taxation.

ARGUMENT

I. The Iowa Statutory Sales Factor Apportionment Formula Does Not, On Its Face, Violate Due Process As Guaranteed By The Fourteenth Amendment To The United States Constitution.

The Iowa sales factor formula is contained in section 422.33(1), Code of Iowa and is a part of a statute regularly enacted by the Iowa legislature. As such, a review of the facial constitutionality of such statute requires this Court -- or any other Court -- to presume that the Iowa formula is valid. Both the trial court and the Iowa Supreme Court recognized this fundamental proposition and its corollary principles (A. 65-66, 115).

Moreover, as the Iowa Supreme Court pointed out, a facial constitutional attack upon a statute requires a showing by the challenger that the statute is unconstitutional "in every conceivable situation which might possibly arise" (A. 131). An examination of the Iowa sales formula contained in section 422.33(1), Code of Iowa, clearly discloses that it is not limited, in application, to non-Iowa manufacturers, like Moorman, but applies to any corporation carrying on its trade or business partly within and partly without Iowa and deriving income from the manufacture or sale of tangible personal property. Hence, the sales formula must be utilized by, among others, corporations manufacturing wholly in Iowa, manufacturing wholly outside of Iowa, manufacturing in Iowa and out of Iowa, and retail and wholesale merchants doing business within and without Iowa. In order for the Iowa sales formula to be facially unconstitutional, it must deprive all such corporate taxpayers of due process of law, and a mere possibility that some of them might be able to show such deprivation is not sufficient. Not all corporations doing business in Iowa are attacking the facial constitutionality of the Iowa formula. Indeed, the amicus brief of the Iowa Manufacturers Association clearly is evidence that there are corporate taxpayers who do not view the Iowa formula as violating their constitutional rights. Thus, Moorman can not, as a matter of law, make an appropriate constitutional attack upon the facial validity of the Iowa formula. Moorman cannot even show concretely that all corporations manufacturing wholly out of Iowa have been deprived of their constitutional rights by the Iowa formula.

The explanation of how the Iowa corporate net income tax operates is dealt with in the Iowa Supreme Court's opinion and is not really controverted by the parties herein (A. 105-106, 116-117). Section 422.33, Code of Iowa imposes the tax upon the net income of Iowa corporations and all foreign corporations "doing business in this state." Hence, the statute, by its terms, requires an income producing nexus in Iowa as a

prerequisite for imposition of the tax. No tax is imposed upon those corporations who merely ship goods into Iowa, but have no nexus here, such as the situation in *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967). Those corporations engaged in a trade or business carried on partly within and partly without Iowa first compute net income derived from interest, dividends, rents, and royalties, and deduct such net income from their overall federal taxable income, as defined in section 422.35, Code of Iowa. The remainder of such net income, if derived from the manufacture or sale of tangible personal property within and without Iowa, is apportioned to Iowa by using the Iowa sales formula. Section 422.33(2), Code of Iowa, provides under the circumstances therein, for use of an alternative formula.

The basic test to determine whether a state tax violates due process guarantees is contained in *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435, 444 (1940):

> "The Constitution is not a formulary. It does not demand of states strict observance of rigid categories nor precision of technical phrasing in their exercise of the most basic power of government, that of taxation. For constitutional purposes the decisive issue turns on the operating incidence of a challenged tax. A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society."

This basic due process test has also been incorporated into apportionment cases. *Norfolk & Western Railway Co. v. Missouri State Tax Commission*, 390 U.S. 317, 325, (1968) (footnote 5):

> " 'So far as due process is concerned the only question is whether the tax in practical operation has relation to

> opportunities, benefits, or protection conferred or afforded by the taxing state. See *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435, 444 [85 L Ed 267, 270, 61 S.Ct. 246, 130 ALR 1129]. Those requirements are satisfied if the tax is fairly apportioned to the commerce carried on within the State.' Ott v. Mississippi Valley Barge Line Co., 336 U.S. 169, 174, 93 L.Ed. 585, 589, 69 S.Ct. 432 (1949)."

Consequently, unless Moorman can demonstrate that the Iowa sales formula does not fairly apportion its income to its activities in Iowa, no due process violation can occur. The stipulated evidence denotes that Moorman does business in Iowa and engages in extensive income producing activities in Iowa (A. 24-25). Its extensive use of salesmen in Iowa as well as its own warehouses allow it to exploit the Iowa market place. The State of Iowa allows corporations to do business, protects them in their business dealings, and provides for an orderly market in which Moorman and other corporations can transact business. The fact of the matter is that Moorman has sufficient contacts with the State of Iowa without which it could not sell approximately 20% of its products, for the years in question, in this state. Thus, for 1968 as an example, Moorman's Iowa activities produced $21,380,320 of gross Iowa sales (Exhibit 8, A. 36).

The foundational premise of the facial due process attack upon the Iowa sales formula by Moorman and its amici allies lies in their unproven assumption, adopted by the trial court but rejected as not true by the Iowa Supreme Court, that the Iowa sales formula taxes 100% of Moorman's net income derived from its Iowa sales of goods wholly manufactured in Illinois. Prior constitutional precedents of this Court conclusively demonstrate that such an unproven assumption does not satisfy a taxpayer's burden of overturning an apportionment formula on its face.

An analysis of prior constitutional apportionment precedents of this Court upholding single and multi-factor formulae will establish that these cases support the facial constitutionality of the Iowa sales formula in the instant case and do not support Moorman's appeal.

In *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920), this Court sustained the constitutionality of a Connecticut income tax statute which apportioned net income on the basis of a single property factor formula. This formula had the effect of apportioning 47% of a Connecticut based manufacturer's net income to Connecticut. An analysis of the evidence disclosed that the Iowa formula would have apportioned about 3.3% of such net income to the taxing state. (R. Item 3, p. 14). This Court stated at 254 U.S. 120-1:

> "The legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It therefore adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the state."

This statement is completely apropos to Moorman in the instant case. This Court would not indulge in speculations and assumptions as to source of income or amount thereof but determined that the record did not disclose any concrete evidentiary showing by the taxpayer that the formula challenged was somehow improper. Contrary to Moorman's argument, this case does not support the assumptions made by Moorman. (Moorman Brief, pp. 30-31).

In *Bass, Ratcliff & Gretton, Ltd. v. State Tax Commission*, 266 U.S. 271 (1924), a New York franchise tax measured by net income apportioned by a single assets factor, containing tangible and intangible property, was attacked upon due process and commerce clause grounds by a foreign-based manufacturer

whose only New York activity appeared to be a branch sales office located therein. It is quite possible that the use of the Iowa formula would have had the effect of apportioning no income to New York. (R. Item 3, p. 16). Economically, arguments could have been made, as Moorman repeatedly does, that the formula merely identified income, but did not apportion it, and that location of sales branch offices or the market place is irrelevant. However, the arguments would have been as invalid in that case as they are in the present case. This Court held that the constitutional questions were controlled "by the decision in *Underwood Typewriter Co. v. Chamberlain*." 266 U.S. 280. And, this Court stated at 266 U.S. 283:

> "There is no evidence in the record as to whether the company received any net income from its New York business, or the amount of the profit and loss on that business, if any, either considered separately or in connection with the manufacturing business carried on in Great Britain."

Note how this statement would preclude an assumption that the Iowa sales formula caused Moorman to be taxed on 100% of its income from its Iowa sales of goods manufactured in Illinois and would preclude the use of assumptions by Moorman to carry its burden of proof. (Moorman Brief, pp. 29-30).

Hans Rees' Sons, Inc. v. North Carolina, 283 U.S. 123 (1930) involved a constitutional attack, upon due process and commerce clause grounds, on the North Carolina single property factor formula as applied to the net income of a North Carolina based manufacturer. Unlike *Underwood* and *Bass*, the taxpayer introduced concrete evidence denoting that its income was derived from three sources, namely, buying profit, manufacturing profit, and selling profit. No speculation or conjecture was involved as to either the source or amount of such profits. This Court simply found that the evidence presented was competent to show that the single property factor formula

should not be applied to this particular taxpayer as it produced arbitrary and unreasonable results in the form of extraterritorial taxation. No such evidence has been offered in the instant case by Moorman. Whether Moorman's manufacturing activities produced a profit or a loss is unknown. It is not even known whether the net income actually taxed by Iowa contains any manufacturing profit at all.

In *Kent-Coffey Mfg. Co. v. Maxwell*, 291 U.S. 642 (1933), the North Carolina single property factor formula was again constitutionally attacked by a North Carolina based manufacturer. This formula apportioned 99.2% of taxpayer's net income to North Carolina whereas the Iowa sales factor would have apportioned .2% (R. Item 3, p. 18). The taxpayer relied upon *Hans Rees'* but such reliance, in view of the lack of an evidentiary showing, was held to be misplaced and the decision that the single property factor formula was constitutionally applied was based upon *Underwood*. Neither the North Carolina Court nor the United States Supreme Court would indulge in the assumption that the formula's effect upon Hans Rees' income would likewise be the same for Kent-Coffey's income, in view of Kent-Coffey's failure to introduce concrete evidence to overturn the formula. The decision in this case clearly refutes the tactics advocated by Moorman in its facial constitutional attack upon the Iowa sales formula.

Norfolk & Western Railway Co. v. North Carolina, 297 U.S. 682 (1936) involved the constitutionality of the North Carolina mileage formula to apportion net income of an interstate railway operating in and out of North Carolina. The railway introduced evidence concerning its operating expenses in North Carolina, but no evidence as to its actual and average gross revenues. This Court refused to speculate what such evidence might have shown. Once again, this Court was simply confronted with a state's apportionment scheme which was not shown by the taxpayer to be constitutionally infirm through

the evidence presented. Moorman's presentation rises to no higher level in the instant case. It should be noted that there is little difference between a mileage formula and a sales formula since a railroad's gross receipts it receives depends upon the mileage it generates. Such mileage has no necessary correlation to the amount of property and labor performed in the taxing state. This case supports the proposition that a sales formula is facially constitutional.

In *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939), this Court had for consideration the validity, upon due process and commerce clause grounds, of a Texas franchise tax in which the tax base was apportioned by a single gross receipts formula, as applied to the taxpayer, a motor vehicle manufacturer, doing no manufacturing activities in Texas. This Court sustained the tax, noting, contrary to Moorman's attempt (Moorman Brief, pp. 24-25) to distinguish it, that "It is much like that upheld in *Bass, Ratcliff & Gretton v. State Tax Commission.*" 308 U.S. 335. Indeed, this Court rejected the very rationale advanced by Moorman and its amici allies, namely, that an apportionment formula based upon geographical location of property is sound but one by sales is not, by expressly noting at 308 U.S. 336:

> "We reject petitioner's contention that constitutionality of state taxation turns on so narrow an issue as whether local assets rather than local gross receipts are used in a taxing formula."

In *Butler Bros. v. McColgan*, 315 U.S. 501 (1942), this Court rejected a due process attack upon the California three factor (property, payroll, sales) formula as applied to the net income of a taxpayer, a merchant. This formula had the effect of apportioning 8.1372% of taxpayer's net income to California whereas the Iowa sales factor would appear to have apportioned 7.57% of such income to that state. (R. Item 3, p. 17). Citing the cases previously discussed herein, including *Ford Motor Co.*, this Court upheld the apportionment formula. This Court was

faced with a factual stipulation as the record evidence to decide whether the California formula was valid. This Court noted that the taxpayer had failed to show "the precise sources of its net income of $1,149,677." No assumptions, hypotheticals, or speculations were indulged in to overcome the presumption of constitutionality of the formula under attack. The taxpayer failed to show by clear and cogent evidence that the challenged formula was invalid.

In the aforementioned cases, taxpayers attacking the constitutionality of a statutory apportionment formula attempted to compare the results reached by the application of the challenged formula and some other method. In no case was such mere discrepancy of results reached between the challenged formula and some other method, per se, held to shift the burden to the state to justify its formula. In each case, this Court carefully inquired into the evidentiary record made in the courts below to determine whether sufficient evidence was presented to overturn the use of the challenged formula. In no case were assumptions and speculations by taxpayers as to source of income or amount allowed. Rather, the presumption was that the formula was valid until shown otherwise and all assumptions were indulged in to support the formula, not to defeat it. In no case were hypothetical examples entertained as satisfying the weighty burden of proof. Indeed, Hans Rees' won its case only by the actual evidence it presented. Clearly, Moorman's contentions and those of its amici attacking the Iowa sales formula can not be squared with the decisions of this Court in the aforementioned cases. Consequently, to presume that the Iowa formula taxes 100% of Moorman's income from its Iowa sales and that the Iowa formula apportions nothing simply would be inconsistent with this Court's decisions. We do not mean to suggest that the Iowa single sales factor formula can never be invalid as applied; only that it is not facially unconstitutional (and not unconstitutional as applied to Moorman's net income). For to hold that the Iowa formula is facially

invalid, as Moorman and its amici suggest, is to indulge in abstractions which this Court has declined to speculate upon. "We cannot deal in abstractions. In this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense." *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 463 (1959). In a number of the aforementioned cases, the amount of net income attributed to the taxing state by the apportionment formula sustained by this Court was greater than would have been the amount so apportioned by the Iowa single sales factor formula. That being the case, it can hardly be seriously contended that the Iowa sales formula is facially unconstitutional. There is no reason to suggest that the instant appeal should be treated differently than its constitutional predecessors by this Court.

Because of the complex nature of interstate business and the resultant inability to segregate the net income base of such business upon a geographical basis, the use of an apportionment formula is mandatory. And given this premise, this Court has never imposed upon the states a uniform apportionment formula, but has allowed the states great leeway in their choice of such formulae. Naturally, not all states will, therefore, adopt the same formula. And, because of the very nature of the undertaking, the formula used need only produce rough approximation, and not precision or even the best possible result. Indeed, as this Court pointed out in *International Harvester Co. v. Evatt*, 329 U.S. 416, 422 (1947):

> "Furthermore, this Court has long realized the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as those of appellant, and has declared that 'rough approximation rather than precision' is sufficient . . . unless a palpably disproportionate result comes from an apportionment . . . this Court has not been willing to nullify honest state efforts to make apportionments."

Therefore, in order to muster a constitutional attack upon a state's apportionment formula, the affected taxpayer has been given a very heavy burden of showing by clear and cogent evidence that the formula is invalid in the concrete factual circumstances which the taxpayer is required to present. *Butler Bros. v. McColgan*, supra; *Norfolk & Western Railway Co. v. North Carolina*, supra.

The aforementioned cases discussed herein contain the constitutional principles followed by the Iowa Supreme Court in analyzing Moorman's due process contentions and the Iowa Court's resolution and rejection of Moorman's arguments is analytically sound (A. 116-132).

On its face, the Iowa sales formula apportions net income to Iowa on the basis of an interstate corporation's business transacted in the Iowa market place – an obvious income producing activity. "The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut, and ending with sale in other states." *Underwood*, supra, at 254 U.S. 120. To argue, as does Moorman, that the Iowa sales factor merely identifies income but does not apportion it is not based upon any constitutional mandate, but is a mere economic theory. This argument is inconsistent with *Underwood* and *Ford Motor Co.*, in particular. In addition, to judically approve such an argument is to place an economic rigidity upon the interpretation of the Constitution by virtually requiring all states to adopt the three factor formula. As Justice Frankfurter stated:

> "We must be on guard against imprisoning the taxing power of the states within formulas that are not compelled by the Constitution but merely represent judicial generalizations exceeding the concrete circumstances which they profess to summarize." *Wisconsin v. J. C. Penney*, 311 U.S. at 445.

As noted, the Iowa sales formula is rationally related to due process requirements and is entitled to a presumption of constitutionality. A state, for example, Illinois, could have enacted a statutory single sales factor, a two factor (sales and property), or a three factor (sales, property, and payroll) formula, to apportion interstate net income. Indeed, Illinois has enacted a three factor formula. Such multi-factor formulae also, on their face, contain income producing factors and, are, thus, entitled to the presumption of constitutionality. Because there is no way, ordinarily, to specifically allocate the profits of a unitary multistate business on a geographical basis, it cannot be assumed that an apportionment formula containing one or more income producing activities is facially unconstitutional, notwithstanding that the apportionment formulae adopted by different states differ either in the factors included or in the computation of included factors. Thus, insofar as Moorman is concerned, there is nothing in the instant case indicating that the Illinois three factor formula apportions more or less net income to Illinois than actually earned there or that the Iowa sales formula apportions more or less net income to Iowa than actually earned in Iowa. While, for due process analysis, it is proper in apportionment cases to engage in assumptions to sustain apportionment formulae, it has never been considered proper to strike down such formulae on the basis of assumptions. Consequently, the cornerstone of Moorman's due process argument, to wit, the Iowa sales formula taxes 100% of Moorman's income from its Iowa sales, being a mere unproven assumption, cannot be and should not be accepted particularly in view of the heavy burden of proof Moorman has to show facial invalidity of an apportionment formula. Moreover, as the Iowa Supreme Court deftly pointed out, Moorman was not taxed upon 100% of such income (A. 134).

There is nothing in the record in this case which discloses that Moorman either proved that Iowa taxed 100% of its net income derived from Iowa sales, that the Director agreed with

such an assumption, or that the net income taxed was clearly derived from Illinois sources. Certainly, the figures contained on pages 12-13 and 27-28 of Moorman's Brief as well as the mathematical gymnastics in its Appendix E do not constitute such proof. Instead, for example, for the year 1968, the stipulated data discloses that Moorman had $97,719,800 of gross sales in all the states it did business in, of which $21,380,320 were attributed to the Iowa market place (Exhibit 8, A. 36). Thus, the record discloses at most that 100% of Moorman's gross income from Iowa sales was, for 1968, $21,380,320. But, Iowa did not levy its income tax upon this figure -- the only record evidence of income from Iowa sales. Rather, after allowance of deductions and application of the Iowa sales factor to Moorman's overall net income as defined in section 422.35, Code of Iowa, Iowa levies its tax upon $1,546,284 of Moorman's net income (Exhibit 8, A. 34). Obviously, the actual income taxed is not 100% of Moorman's income from Iowa sales, but merely a very small fraction thereof. To say, therefore, that Iowa taxed 100% of Moorman's net income from Iowa sales is to indulge in pure speculation -- and not very good speculation. There is nothing in the record of this case to show Illinois or any other state taxed any part of this $1,546,284. These same conclusions are applicable for Moorman's other tax years involved in this case.

The trial court agreed with Moorman that the Iowa formula taxed 100% of Moorman's net income from Iowa sales (A. 76-78). Moorman contends that the Iowa Supreme Court made no direct response to the findings of the trial court that the income which Iowa taxed was greatly attributable to Illinois plant and personnel inputs and was out of all reasonable proportion to business done in Iowa (Moorman's Brief, p. 22; A. 76, 77). As noted these findings are based upon the faulty premise that Iowa was taxing 100% of such income which the Iowa Supreme Court did respond to (A. 134). Moreover, it is not known, on the record herein, how much of such income, if

any, is actually attributable to the manufacturing process in Illinois. At most, the record in this case, as the Director pointed out in his Motion to Dismiss, only disclosed that, for example, 1968, based upon the abstract interplay of the Iowa and Illinois apportionment formulae, Iowa taxed 21.88% of Moorman's computed net income under Iowa law and Illinois taxed 41.76% of income not considering Illinois sales (Motion to Dismiss, p. 14, footnote 13). In view of this Court's pronouncements that rough approximation produced by formula apportionment is sufficient, the Iowa formula would still be facially valid even if a very small, but not disproportionate share, of Moorman's income taxed by Iowa could be actually attributed to Illinois. Exact precision in taxation is not required.

That Moorman relies upon hypothetical situations to satisfy its burden of showing the facial unconstitutionality of the Iowa formula is clearly demonstrated by Moorman's statement contained in its Petition For Rehearing to the Iowa Supreme Court:

> "Furthermore, facial unconstitutionality must be proven by the use of hypotheticals as was done in *General Motors*, where the facial invalidity of a regulation was at issue. In no other way can a litigant negative every reasonable basis which may support the statute. In the case before this Court, Moorman has proven the facial unconstitutionality of § 422.33(1)(b) by the use of hypotheticals, none of which have been challenged." (A. 151).

If this statement by Moorman was a correct exposition of the constitutional standards involved in a due process attack upon an apportionment formula, there would be little or nothing to present in the way of an evidentiary attack upon such formula. All that would be necessary in apportionment cases is the production of an economist's brief – as, indeed, has been presented by Amici Baumol et al. Thus, the constitutionality of apportionment formulae would depend upon the acute and

powerful economic intellect, not upon the constitutional standards evolved by this Court in apportionment cases.

It is axiomatic that hypotheticals form no basis for constitutional attacks upon statutes. *United States v. Raines*, 362 U.S. 17 (1960). In particular, the use of hypotheticals has never been condoned by this Court to show the invalidity of apportionment formulae. The above quoted statement by Moorman is so obviously inconsistent with *Underwood Typewriter Co. v. Chamberlain*, supra; *Bass, Ratcliff & Gretton Ltd v. State Tax Commission*, supra; *National Leather Co. v. Massachusetts*, 277 U.S. 413 (1928); *Hans Rees' Sons, Inc. v. North Carolina*, supra; *Kent-Coffey Mfg. Co. v. Maxwell*, supra; *Norfolk & Western Railway Co. v. North Carolina*, supra; *Ford Motor Co. v. Beauchamp*, supra; *Butler Brothers v. McColgan*, supra; *International Harvestor Co. v. Evatt*, supra. This statement is clearly inconsistent with this Court's refusal to deal with abstractions in *Northwestern States Portland cement Co. v. Minnesota*, supra, 358 U.S. 463. This statement, in essence, is an admission by Moorman that it cannot show by concrete facts that the Iowa formula is facially unconstitutional.[1]

Moorman states in its brief that the "only rationale for taxes is government services" (Moorman Brief, p. 17). The Director agrees. "The simple but controlling question is whether the state has given anything for which it can ask return." *Wisconsin v. J. C. Penney Co.*, supra, 311 U.S. 444. But, then Moorman contends that imposition of income taxes, to be consistent with the above rationale, must be quantitatively related to the property and employees of the taxpayer located in the taxing state and the location of the market place in which

1. The Court's attention is directed to the case quotes on pages 11-12 of the Director's Motion To Dismiss. The use of hypotheticals as an adequate showing of either facial unconstitutionality or unconstitutionality as applied cannot be squared with the quotations from these cases. The principles contained in these cases were followed in this case by the Iowa Supreme Court but ignored by the trial court.

sales are made is irrelevant. Not only does this point lack merit, but this Court in essence rejected it, for purposes of approving an unapportioned gross receipts tax in *Standard Pressed Steel Co. v. Washington*, 419 U.S. 560 (1975). While it is undisputed that Moorman has significant amounts of people and property in Iowa, even if Moorman had no property in Iowa and few salesmen, it would be a sufficient beneficiary of government services so as to be required to pay Iowa income tax on income it earned from the Iowa market place. Such a result would be no more onerous – and probably less – than this Court's decision in *Standard Pressed Steel Co.* Moorman's argument that an income tax is facially invalid unless an apportionment formula considers relative quantities of property and people is undermined by this Court's statement in *Ford Motor*, supra at 308 U.S. 336:

> "We reject petitioner's contention that constitutionality of state taxation turns on so narrow an issue as whether local assets rather than local gross receipts are used in a taxing formula."

Moorman attempts to distinguish *Ford Motor* as well as other cases cited by the Iowa Supreme Court in support of the facial constitutionality of the Iowa sales formula. (Moorman Brief, pp. 24-25). Indeed, Moorman contends that *Underwood*, *Kent-Coffey*, and *Bass* support the trial court's decision.[2] In the gross receipts apportionment formula *Ford Motor* case, this Court relied upon its holding in *Bass*, sustaining a single assets factor formula. In *Bass*, this Court held that the constitutionality of the assets formula was controlled by the *Underwood* decision sustaining a single property factor. *Kent-Coffey* was wholly decided by this Court on the basis of *Underwood*. In the three factor case of *Butler Bros*, the *Ford Motor* case was cited with approval and as support for this Court's decision to sustain such formula.

2. The trial court felt such cases were of little significance and did not rely upon them (A. 85).

Therefore, regardless of the type of tax or formula involved, this Court has relied upon all such cases and has never sought to distinguish them. Also, *Underwood* which upheld an apportionment formula as applied to an instate manufacturer was used to control the decision in *Bass* relating to apportionment of income of a manufacturer doing no manufacturing in the taxing state. Consequently, it is clear that these cases support the conclusion of the Iowa Supreme Court that the Iowa sales formula is facially constitutional. Moorman's analysis of these cases that they support its appeal herein is clearly incorrect.

In its brief, Moorman, unlike its Jurisdictional Statement, purports to state that it now makes no demand upon this Court to prescribe any specific formula to apportion income (Moorman Brief, p. 31). A closer reading of this Brief discloses that Moorman considers a single property factor facially "sound" (Moorman Brief, p. 25) and, obviously, a three factor formula.[3] In this connection, Moorman concedes that such formulae, which could apportion more income to Iowa than under the Iowa taxing scheme, are facially valid, a self-defeating admission insofar as facial constitutionality is involved.[4] Clearly, the use of such formulae by Moorman would apportion less computed Iowa net income pursuant to Iowa Code section 422.35 than would the Iowa sales formula because of Moorman's factual situation. However, Moorman attacks the weighted 3 factor formulae (double weight on sales) of Florida, Wisconsin, New York, and Massachusetts. (Moorman Brief, p. 39). The stipulated data will disclose that such facially valid weighted three factor formulae applied to the Iowa net income base without a federal tax deduction would have apportioned $241,409 more

3. Both in its Jurisdictional Statement and in its Brief, Moorman claims to have used the three factor formula contained in the Uniform Division of Income for Tax Purposes Act. The Director commented upon this point in his Motion to Dismiss (Motion to Dismiss, p. 3, footnote 1).

4. See prior discussion in this brief on comparison of Iowa formula with formulae upheld in these cases.

net income of Moorman to Iowa than the Iowa tax scheme (Exhibit 8, A. 52). Consequently, Moorman purports to accept a single property factor formula and its three factor formula, but not much else. Thus, Moorman, in essence, is attempting to make the Constitution a strict formulary by "graciously" accepting the equally weighted three factor formula. Such a view is clearly inconsistent with any apportionment case ever decided by this Court and cannot be squared with the due process principles consistently formulated by this Court over many years and duly adhered to by the Iowa Supreme Court in this case (A. 130).

Moorman's evidence, which it claims the Director did not rebut, rose no higher than a showing that its computed three factor formula apportioned less net income from the sale of tangible personal property attributed to Iowa than would the Iowa sales formula. To this, the Iowa Supreme Court made appropriate response:

> "However, the mere fact application of the single factor formula results in a larger percentage being used for ascertaining the Iowa portion of the corporation's net income than would application of some other type of formula does not render the apportionment provision of the Iowa corporate income tax law facially unconstitutional in violation of due process clauses of the federal and state constitutions. Such evidence alone does not establish that the difference between the two figures represents either double taxation or a taxation of extraterritorial values. Fairness is not equated with absolute precision." (A. 131-132).

Under the constitutional principles which this Court has evolved and expounded in apportionment cases, the taxpayer seeking to invalidate an apportionment formula must come forward with clear and cogent evidence to negate the use of such formula. Once that occurs, the State must rebut such evidence or lose. *Norfolk & Western Railway Co. v. Missouri*

State Tax Commission, 390 U.S. 317 (1968). But, the State is not required to inform a taxpayer how to invalidate a statutory apportionment formula and until the taxpayer has come forward with such evidence, the State can merely stand on its formula. Nowhere is this more clearly demonstrated than in *Bass*, *Underwood*, *Ford Motor*, and *Butler Bros*, in which the State never presented evidence to rebut the showing made by the taxpayer. Indeed, the evidence produced by the taxpayer and not rebutted by the State in *Butler Bros* was far more extensive in concrete terms than Moorman presented. The mere fact that an evidentiary showing can be made to invalidate a single factor formula under concrete circumstances does not render the formula facially invalid under all conceivable circumstances. Nowhere is this point more clearly expressed than by the decision in *Underwood* upholding the single property factor, later decision in *Hans Rees'* invalidating the property formula as applied, and subsequent decision in *Kent-Coffey* upholding the property formula. The State is also not required to rebut assumptions and hypotheticals contrived by Moorman and its amici (although we have pointed out the underlying fallacies of them). The Director has, however, demonstrated herein that Moorman was not taxed upon 100% of its income from Iowa sales -- a factual conclusion adopted by the Iowa Supreme Court (A. 134).

Moorman contends that the Iowa sales factor subsidizes exports and imposes a tariff upon imports in violation of due process. (Moorman Brief, p. 8). The same contention is made to assert that the Iowa formula violates the commerce clause. (Moorman Brief, p. 15). The Director believes that such a contention is addressed to a question of discrimination against interstate commerce. In any event, the Director will deal with this issue in the commerce clause portion of his brief, incorporating herein by reference his discussion thereof.

The Iowa Supreme Court found that the Iowa "formula in

question meets the due process requirement of attempting to fairly allocate the corporation's income" (A. 132). It is respectfully submitted that the Iowa Court's decision that the Iowa formula is not facially violative of due process is amply supported by reason and law and should be sustained by this Court. No showing has been made that the Iowa formula, on its face, caused or produced extraterritorial taxation or subjected to Iowa tax Moorman's income out of all reasonable proportion to Moorman's business transacted in Iowa.[5]

II. The Iowa Statutory Sales Factor Apportionment Formula Does Not, On Its Face, Violate the Commerce Clause of the United States Constitution.

The Iowa Supreme Court noted:

> "The considerations applicable to the resolution of a due process challenge to an apportionment formula are substantially similar to those utilized in assessing the validity of that formula with respect to the commerce clause. Extraterritorial taxation is constitutionally defective 'both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due.' Norfolk & W.Ry. Co. v. Missouri State Tax Com'n, supra, 390 U.S. at 325, 88 S.Ct. at 1001, 19 L.Ed.2d at _____." (A. 132).

It is a violation of the commerce clause (Article I, Section 8, Clause 3) of the United States Constitution to subject interstate commerce to the risk of multiple state taxation and to discriminate against interstate commerce in favor of locally based industry through state taxation. *Standard Pressed Steel Co. v. Washington*, supra; *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318 (1977).

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5. In addition to Due Process, Moorman argued the Iowa formula violated a fundamental principle of federalism. This issue has never been raised in any previous stage of these proceedings. It also has no merit.

Like the arguments made for due process violation, the foundation of Moorman and its allied amici's contentions that the Iowa sales formula facially violates the commerce clause rests upon the hypothesis that the Iowa formula taxes 100% of the income derived from Iowa sales of goods manufactured in Illinois. The Director's analysis and rebuttal of this premise in the due process portion of his brief are also incorporated herein by reference. And, such an unproven hypothesis cannot satisfy Moorman's weighty burden of showing by clear and cogent evidence that the Iowa formula is facially invalid. Multiple taxation, in the constitutional sense, is not shown merely because the Iowa apportionment formula does not guarantee precision. As long as roughly approximate results exist, this Court has not striken an apportionment formula upon commerce clause grounds.

The presence of multiple state taxation of Moorman's net income cannot rest upon an abstract assumption that Iowa taxed or risked the taxation of 100% of income derived from Moorman's Iowa sales and cannot rest upon the abstract interplay between the Iowa and Illinois apportionment formulae (Moorman Brief, pp 10-13). Indeed, as this Court stated in *Northwestern States Portland Cement Company v. Minnesota*, 358 U.S. 450, 463:

> "There is nothing to show that multiple taxation is present. We cannot deal in abstractions. In this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense. This they have failed to do."

Likewise, Moorman has failed to demonstrate that multiple taxation is present in this case.

The amicus brief of the multistate tax commission and attorney general of the State of Oregon indicates that states, other than Iowa, have constitutionally exerted their taxing

power over corporations with unitary subsidiaries by including in the net income base subject to formula apportionment the entire business net incomes of the parent and subsidiary corporations (Commission Brief, p. 5). The Director did not require Moorman to file an Iowa consolidated return and did not apportion to Iowa any of the net income of Moorman's subsidiaries (A. 23). Thus, Moorman has not demonstrated in this case that all of its unitary apportionable net income was subjected to taxation by Iowa to the extent other states so tax or can tax Moorman. That being the case, there should be no inference of overlapping state taxation of Moorman's unitary income because of the Iowa formula.

Moorman contends that the tax base is irrelevant to considerations of multiple state taxation involving an apportionment formula (Moorman Brief, pp. 13-15). Yet, the tax base can be relevant to disclose that a state has not exceeded the full extent of its constitutional authority in the practical operation of the tax. In *Standard Pressed Steel Co. v. Department of Revenue*, supra, this Court considered the constitutionality of the Washington business and occupation tax levied upon the unapportioned gross receipts derived by the taxpayer from interstate sales to a customer located in Washington. An employee of the taxpayer was constantly in Washington, but did not take any sales orders from the Washington customer who sent such orders outside of Washington for acceptance by the taxpayer. This Court sustained the levy of the tax on the taxpayer's gross income from such interstate sales on the basis of *General Motors Corp. v. Washington*, 377 U.S. 436 (1964). This Court rejected the taxpayer's contention that a risk of multiple taxation was demonstrated at 419 U.S. 563:

> "We noted in General Motors that a vice in a tax on gross receipts of a corporation doing an interstate business is the risk of multiple taxation; but that the burden is on the taxpayer to demonstrate it, id., at 449, 12 L.Ed 2d 430. The corporation made no such showing there. Nor is any

effort made to establish it here."

In the instant case, to repeat, the stipulated data discloses that Moorman made Iowa sales in 1968 of $21,380,320 (Exhibit 8, A. 36). Under *Standard Pressed Steel*, Iowa could have taxed this amount without risking double taxation, but instead, for that year, Iowa taxed $1,546,284. Moorman has made no showing where this $1,546,284 was actually earned. But, at most, it inferentially represents a mere fraction of the $21,380,320 and it obviously cannot be considered to represent 100% of the income derived from Iowa sales by Moorman. Consequently, the Iowa Supreme Court correctly concluded that Iowa did not tax 100% of Moorman's income from Iowa sales in view of the Iowa tax base. If Iowa, in 1968, could have levied an unapportioned gross income tax upon Moorman and other corporations similarly situated why cannot Iowa levy its tax upon a lesser apportioned net amount?

Moorman makes an irrelevant argument to the effect that the reason why the tax base is irrelevant is because a high tax base produces a low tax rate and a low tax base produces a high tax rate (Moorman Brief, p. 14). The wisdom of having a high or low tax base or tax rate is not of concern here. "The wisdom of state net income taxes is one of state policy not for our decision." *Northwestern States Portland Cement Company v. Minnesota*, 358 U.S. 462.

As noted in the due process portion of this brief, Moorman has never demonstrated, concretely, that the Iowa sales formula caused extraterritorial taxation to be visited upon Moorman or any other corporation. In view of assumptions and presumptions used in apportionment cases, it must be assumed that the Iowa formula would reach profits reasonably attributable to Iowa. Logically, therefore, there is no basis for concluding that the Iowa formula causes actual or a risk of multiple taxation because of enactment of this formula by the Iowa legislature. Moorman's posi-

tion is that the Iowa formula, regardless of the facts, inherently taxes profits earned outside of Iowa, without proof such is the case, in every conceivable situation imagined. This position is obviously inconsistent with this Court's constitutional apportionment case precedents and principles therein, in some of which more income was actually apportioned to the taxing state than would have been by using the Iowa formula. No multiple taxation or discrimination against interstate commerce was found in those cases. The mere possibility that there may be come multiple state taxation affecting particular taxpayers at various times under some conceivable circumstances would not show the Iowa formula facially invalid.

Moorman contends that the Iowa sales formula subsidizes exports and imposes a tariff on imports, thereby discriminating against non-Iowa based manufacturers by granting Iowa based manufacturers a competitive advantage because non-Iowa based manufacturers are subjected to multiple taxation (Moorman Brief, pp. 15-17). Like all of its other arguments, this argument of Moorman's concerning alleged discrimination against interstate commerce rests upon the faulty premise, refuted by the Iowa Supreme Court, that 100% of Moorman's income derived from its Iowa sales is apportioned to and taxed by Iowa. It is clear that, on its face, the Iowa income tax scheme is not discriminatory. Section 422.33, Code of Iowa, which imposes the tax, sets the tax rates, and provides for apportionment of interstate income, does not, on its face, provide different and discriminatory treatment for local corporations or foreign corporations similar to Moorman's situation. Section 422.35, Code of Iowa, which defines the tax base does not grant a different base to Iowa corporations and foreign corporations. Insofar as the Iowa apportionment formula is concerned, it applies to all corporations selling goods in the Iowa market place and earning income there. Hence, the Iowa taxing scheme, standing alone, does not constitute a discrimination against interstate commerce nor an unconstitutional risk of multiple

taxation. Since the formula applies to all interstate corporations doing business in Iowa apportioning only the portion of their income earned here and since Section 422.33, Code of Iowa, taxes 100% of a corporation's income earned wholly intrastate in Iowa, no facial discrimination against interstate commerce exists. Clearly, a reading of the Iowa net income tax statute in Section 422.33, Code of Iowa, will not disclose, facially, any practical discrimination against interstate commerce of any type.

Moorman, however, does not simply consider whether the Iowa formula, standing alone, creates a risk of multiple taxation and discrimination against interstate commerce. Moorman concludes the Iowa sales formula violates the commerce clause by granting Iowa based corporations competitive advantages on the basis of the abstract interplay between the Iowa sales formula in the context of other states', notably Illinois, use of the three factor formula. Again, of course, this contention indefensibly assumes that Iowa taxed 100% of the income derived from Iowa sales and assumes there must be overlapping taxation. This conclusion is wrong for the further reason that it allows the configuration of laws of other states, in the abstract, to dictate the constitutionality of the Iowa law. We know of no case where this Court has stricken, on commerce clause grounds, an apportionment formula or any tax scheme on such a basis.

Consider, for example, the situation if the only state which had enacted an income tax was Iowa. The Iowa sales formula would apportion income of all interstate corporations to Iowa. Next, Illinois decides to impose an income tax apportioned by a destination sales formula. No multiple taxation or discriminatory taxation would arise.[6] Then, all states impose income taxes

6. This is conceded in the Amicus Brief of the Council of State Chambers of Commerce (COST Brief, p. 8, footnote 7).

apportioned for interstate commerce by the destination sales factor. Again, no commerce clause problems. But, suppose one state, i.e. Illinois, decided to change its law and apportion income by a three factor formula. Under Moorman's theory of commerce clause violation, the Iowa sales factor now violates the Constitution because of the laws enacted by the State of Illinois or perhaps the Illinois law is invalid because it is so different from other state formulas. But, there was no multiple taxation or discrimination before Illinois adopted the three factor formula. Consequently, Illinois, not Iowa, under Moorman's argument carried to its logical conclusion, created a risk of multiple taxation. The Director is not saying herein that the Iowa sales formula or the Illinois three factor formula actually create a risk of multiple state taxation. The point is simply this: If the facial constitutionality of the Iowa sales formula concerning discrimination against interstate commerce is to be dictated by legislatively created tax formulae adopted in other states, then it would be impossible for the states to tax net income derived from interstate commerce except by the rigid exact adoption of the same tax scheme including formulae, base, and rates. Further, the first state to adopt an income tax and apportionment formula dictates to the other states to conform their tax schemes thereto or lose them through the device of discriminatory multiple taxation. The wide leeway this Court has afforded the states in their choice of apportionment formulae would disappear. While not a commerce clause precedent, this Court put it well in *Austin v. New Hampshire*, 420 U.S. 656, 668 (1975):

> "Nor, we may add, can the constitutionality of one state's statutes affecting nonresidents depend upon the present configuration of the statutes of another state."

Under Moorman's theory of this case, the Constitution would become the very formulary this Court held it was not in *Wisconsin v. J. C. Penney Co.*, supra, and the configuration of

statutes in other states would dictate the facial constitutionality of the Iowa sales formula, contrary to the above principle enunciated in *Austin*. Moorman's analysis that the Iowa sales formula imposes a tariff upon imports and subsidizes exports is unsound because the Iowa formula, standing alone, cannot have that effect. As long as Iowa properly exercised its taxing power, a commerce clause violation cannot depend upon how Illinois or any other state properly exercises its taxing powers.

The fact of the matter is that Moorman's complaint that it is subjected to different state apportionment formulae raises a political, not a constitutional, question. In this regard, it is not irrelevant to note that Congress, in which the commerce power is placed by the Constitution, has frequently addressed the question of providing for a uniform net income tax apportionment formula and each time has refused to impose upon the states the straightjacket demanded by those who are unable to find in the Constitution's commerce clause support for the exclusivity of the formulae they expouse. See, e.g. S. 1245, 93rd Cong. 1st Sess. (1973); H.R. 1538, 92nd Cong., 1st Sess. (1971); H.R. 669, 95th Cong. 1st Sess. (1977).

Moorman, in attacking the facial constitutionality of the Iowa formula, must negative every reasonable basis which might support the formula. Its attempt to do so by hypotheticals has never been considered by this Court as acceptable, but such tactics have been rejected. Therefore, its assertion that the Iowa formula subsidizes exports and imposes a tariff upon imports is unproven and must necessarily fail. There is no basis for a conclusion that the Iowa formula constitutes "protectionist" legislation for Iowa based manufacturers. It would be an extremely marginal situation to find an Iowa-based manufacturer not selling goods in the Iowa market place. Faced with the impossibility of specifically allocating an interstate corporation's net income on a geographical basis, the Iowa legislature could have concluded that all corporations doing business in

Iowa and exploiting the Iowa market place should apportion net income which they derive in all states they do business in on the basis of sales and that such an apportionment would be fair to Iowa-based and non-Iowa based corporations. Such a determination by the Iowa legislature is clearly consistent with the cases cited herein approving single and multi-factor formulae. It has not been rebutted by Moorman.

Moorman and its amici rely heavily upon this Court's decision in *General Motors Corporation v. District of Columbia*, 380 U.S. 553 (1965). They claim that this case fully supports their contention that the Iowa formula is facially unconstitutional and that a showing of such unconstitutionality can be made by assuming that Iowa taxes 100% of the income Moorman derives from its Iowa sales and by demonstrating hypotheticals. These contentions should be examined in light of what this Court decided in *General Motors*, the statutory provisions involved, and what this Court did not decide. In that case, the taxpayer, a manufacturer of motor vehicles outside of the District of Columbia and a seller thereof in the District, challenged upon constitutional and statutory grounds a regulation promulgated by the District Commissioners to apportion net income to the District by a single sales factor formula. The Court of Appeals for the District of Columbia held that the regulation was consistent with the general statute providing for no specific formula but authorizing the Commissioners to promulgate one and that the regulation was constitutional (336 F.2d 885). This Court reversed that decision "without reaching the constitutional questions presented." 380 U.S.555. While critical of a single sales factor formula, this Court noted that it has never attempted to define one exclusive apportionment formula for the states to use. 380 U.S. 561. No position on the constitutionality of a single sales factor formula was taken – none at all. "We of course do not mean to take any position on the constitutionality of a state income tax based on the sales factor alone." 380 U.S. 561. Instead, this Court found that the District formula was unsup-

ported by the statute. Thus, what this Court was actually doing was determining that the formula adopted by the District was not consistent with the legislative intent of the District statute. That statute not only provided that the net income of multistate corporations must be fairly attributable to the trade and business engaged in the District, but required the Commissioners, in exercising their discretion in promulgating a regulation, to adopt an apportionment formula to include factors related to all portions of the corporation's business within and without the District. 380 U.S. 557. This point was correctly recognized by the Iowa Supreme Court in this case (A. 130). In *General Motors*, therefore, this Court was not faced with the question of the facial constitutionality of a statutory single sales factor formula and because the case was decided upon nonconstitutional grounds and, thus, merely involved the question of whether the exercise of administrative action was supported by the enabling statute, this Court could and did find it necessary to use hypotheticals and assumptions to depict how the single sales factor the Commissioners adopted simply did not do what the statute required, namely, to consider in the formula the fact that General Motors was engaged in manufacturing activities outside of the District, whether those activities actually produced any net income for General Motors or not. This Court declined to promulgate an apportionment formula for the Commissioners and left that action to them. 380 U.S. 562. This Court approved of single property factor formulae and a three factor property-payroll-sales formula. No finding by this Court was made that, in fact, the sales factor formula violated the principles embodied in the due process and commerce clauses.

The Court's decision in *General Motors* surely does not relieve a taxpayer challenging the constitutionality of the Iowa single sales factor formula of the very heavy burden to demonstrate beyond a reasonable doubt by clear and cogent evidence that the formula is invalid. The decision does not

sanction a showing of unconstitutionality upon the hypothesis that Iowa taxed 100% of Moorman's income derived from its Iowa sales when, in fact, there is no evidence of this and what evidence there is compels a contrary conclusion. Indeed, as the Court of Appeals pointed out, there was no unity of agreement among economists as to the rational impact of a sales factor or even as to the factors which should be part of an apportionment formula. 336 F. 2d 899. This is all the more reason for concluding Moorman has not shown the facial invalidity of the Iowa sales formula and for this Court not to facially condemn such formula. The constitutional principles expounded by this Court in prior constitutional precedents were not overruled in *General Motors*. Application of those principles, as the Iowa Supreme Court correctly observed, compel the conclusion that the Iowa sales formula is facially constitutional and no commerce clause violation has been demonstrated in this case.

III. The Iowa Statutory Sales Factor Apportionment Formula Does Not, On Its Face, Violate Equal Protection As Guaranteed By the Fourteenth Amendment To The United States Constitution.

Once again, by the use of hypotheticals (and extreme ones at that), Moorman attempts to show constitutional transgression. (Moorman Brief, p. 33). No evidence is introduced on this constitutional issue of equal protection. In considering Moorman's facial equal protection attack upon the Iowa formula, all presumptions must be indulged in to support the validity of the formula and Moorman must negate all conceivable bases which support the statute. Quite clearly, Moorman has not done this, for as the Iowa Supreme Court noted:

> "Moorman's only attempt to demonstrate the unreasonableness of the classification contained in section 422.33(1)(b) is with reference to admittedly 'extreme' hypothetical situations. Such a tactic clearly does not establish the classification is unreasonable." (A. 137).

Moorman's equal protection argument is, in substance, no different than its due process and commerce clause contentions. The gist of this argument is that the abstract interplay of the Iowa sales formula with those three factor formulae used by other states provides benefits to Iowa businesses unavailable to Moorman. No evidence was introduced on this point. Indeed, Moorman did not even bother to point out its competitors who were the alleged recipients of such advantages, all caused by the Iowa sales formula. [7] It is inconceivable that a corporation with Iowa activities as extensive as Moorman receives less benefits than Iowa based corporations. All corporations doing business in Iowa are the recipients of an orderly market provided by Iowa and all corporations receive protection from Iowa in engaging in such Iowa business.

Historically, this Court has refused to declare acts of Congress or state legislatures unconstitutional on the basis of hypothetical cases. *United States v. Raines*, 362 U.S. 17; *New York v. O'Neil*, 359 U.S.1 (1959). Therefore, it would be entirely consistent with such cases for this Court to refuse to find a facial equal protection infirmity on the basis of the hypothetical argument presented by Moorman in this case.

In *Madden v. Kentucky*, 309 U.S. 83,88 (1940), this Court stated:

> "It has, because of this, been pointed out that in taxation, even more than in other fields, legislatures possess the greatest freedom in classification. Since the members of a legislature necessarily enjoy a familiarity with local conditions which this Court cannot have, the presumption of constitutionality can be overcome only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons and classes. The burden is on the one attacking the legislative arrangement to negative every conceivable basis which might support it."

Moorman has not satisfied its burden as disclosed in *Madden*.

No taxing scheme need be perfect to pass constitutional muster. In *San Antonio School District v. Rodriques*, 411 U.S. 1,41 (1973), this Court stated:

> "No scheme of taxation, whether the tax is imposed on property, income, or purchases of goods and services, has yet been devised which is free of all discriminatory impact. In such a complex arena in which no perfect alternatives exist, the court does well not to impose too rigorous a standard of scrutiny lest all local fiscal schemes become subjects of criticism under the Equal Protection Clause."

Consequently even if a competitor of Moorman was based in Iowa, did all of its manufacturing here, and exported all of its goods out of Iowa, such a stituation would not facially invalidate the Iowa sales formula. To say that it would requires an iron rule of equal taxation to satisfy equal protection whereas no such iron rule has ever been required, but in fact rejected, by this Court.

On its face, Section 422.33, Code of Iowa classifies all corporations doing business in Iowa exactly alike with respect to calculation of tax base, apportionment formula, and rate of taxation. No class of foreign corporations manufacturing and selling tangible personal property is singled out for treatment different than any such corporations based in Iowa. Moorman, by its own admission, does not come within the extreme situations it hypothesizes in its Brief. Thus, the Iowa sales formula does not facially violate equal protection.

---

7. There is nothing in the record in the present case to show that such companies, as listed by Moorman in its two hypothetical situations, are engaged in Iowa in such activities (Moorman Brief, p. 33).

IV. The Application Of The Iowa Statutory Sales Factor Formula To Moorman Is Not Unconstitutional.

Moorman contends that if the Iowa sales formula does not facially violate due process, commerce clause and equal protection, it is invalid as applied to Moorman. In this regard, Moorman essentially posits the same arguments which it made for facial constitutionality and relies upon the same stipulated data (Moorman Brief, p. 36). But, that data rises to no higher level than that Moorman's three factor formula would result in less net income, as computed under Section 422.35, apportioned to Iowa than would the use of the Iowa sales formula. That data does not show that Moorman was subjected to multiple taxation, discrimination, or extraterritorial taxation based upon the assumption that Moorman was taxed upon 100% of its income derived from its Iowa sales. The Iowa Supreme Court correctly found this assumption not to be the fact. The only evidence in the record denoting 100% of Moorman's income from Iowa sales consists of *gross* income which for 1968 as an example was $21,380,320 whereas the Iowa apportioned net income for 1968 only attributed $1,546,284 of Moorman's overall federal taxable income to Iowa (Exhibit 8, A. 34,36). For the other tax years in question, Moorman's net income subject to tax was always less than 100% of its income from Iowa sales (A. 34,36). The Iowa Supreme Court correctly concluded that Moorman could not possibly have been subjected to Iowa tax on 100% of its income from Iowa sales (A. 134). The Iowa Court correctly concluded:

> "No evidentiary justification is provided for a conclusion Moorman is somehow different from those corporations legitimately subject to the provisions of section 422.33(1)(b). In the absence of such evidence Moorman has not made out a sufficient case for overturning on constitutional grounds the application of the Iowa single-sales factor formula to its net income." (A. 139).

In *Bass, Ratcliff & Gretton Ltd. v. State Tax Commission*, supra, at 266 U.S. 283, this Court stated with reference to a manufacturing corporation in the same situation as Moorman:

> "There is no evidence in the record as to whether the company received any net income from its New York business, or the amount of the profit and loss on that business, if any, either considered separately or in connection with the manufacturing business carried on in Great Britain."

In *Norfolk & Western Railway Co. v. North Carolina*, supra, 297 U.S. 688, this Court stated:

> "A finding that the statute, though fair upon its face, is oppressive toward the railway in its practical operation cannot rest upon so fragmentary and partial a showing of facts. We must bear in mind steadily that the burden is on the taxpayer to make oppression manifest by clear and cogent evidence."

There is no "clear and cogent evidence" in this case that the Iowa sales formula visits upon Moorman violations of its constitutional rights as alleged by producing extraterritorial taxation, multiple taxation, or discrimination. Such a showing cannot be made, as a matter of constitutional law, by limiting the inquiry to a comparision of the apportionment percentages of the Iowa sales formula and Illinois three factor formula in the abstract, ignoring Moorman's income-producing activities in all states whereas it is the overall net income derived therefrom which is subject to apportionment and not merely gross income less deductions pinpointed to Iowa and Illinois, failing to consider or point out the profitability of Moorman's operations in all states, failing to point out the precise jurisdictional sources of Moorman's income in all states, failing to consider Moorman's tax bases computed for all states, assuming that an apportionment formula must contain geographical calculations of capital and labor, assuming Moorman was taxed by the Iowa formula on

100% of its income derived from Iowa sales when it was not, and speculating by hypotheticals that the Iowa sales formula gives direct commercial advantages to Iowa-based companies and penalizes imports of foreign corporations. Such is Moorman's constitutional attack both from the standpoint of the facial validity of the Iowa formula and validity as applied to Moorman's net income. Clearly, that attack is defective.

V. Reversal Of The Decision Of The Iowa Supreme Court Would Create A Constitutional Formulary Contrary To The Respect Shown By This Court Toward State Taxation.

This Court, historically, has refrained from requiring the states to pursue any specific apportionment formula. Moreover, "there is nothing in the constitution which requires a state to adopt the best possible system of taxation." *New York v. Latrobe*, 279 U.S. 421 (1929). The Supreme Court of Colorado aptly stated in *General Motors Corp. v. Colorado*, 181 Colo. 360, 367, 509 P.2d 1260, 64 (1973):

> "It was not the trial court's function, nor ours here, to decide which formula was the more economically sound. This is a policy decision for the legislature."

In analyzing the opinions of this Court in apportionment cases, the Iowa Supreme Court stated:

> "As noted, in its opinions in this area the Supreme Court has recognized: (1) the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as the unitary business under consideration here; (2) rough approximation rather than mathematical precision is sufficient; (3) the heavy burden cast upon the taxpayer in challenging a legislative enactment on constitutional grounds; and (4) the utmost leeway must be given the states both in their choice and application of formulae in this connection as long as basic considerations of due process and equal protection are observed." (A. 130)

The above constitutional principles expounded and painstakingly formulated by this Court over many years would be jettisoned if the Iowa Supreme Court's decision is reversed in this case. Moorman really wants this Court to imprint the equally weighted three factor formula as the exclusive one in the Constitution (Moorman Brief, pp. 37-40). In essence, according to Moorman and its economist allies, no other formula is economically sound and the taxing power of the states should be imprisoned within the three factor formula provided in the Uniform Act. This Court has never made such an imposition upon the states in pursuing their fiscal policies and has consistently sustained diverse apportionment formulae. Such decisions by this Court in those cases have not created a detriment to free trade among the states and there is nothing to suggest that the affirmance of the decision of the Iowa Supreme Court in the present case would be detrimental as alleged. The argument that such a detriment would exist many be appropriate for congress to consider as a matter of wisdom of state income tax laws affecting interstate commerce, but it should be rejected in this judicial forum.

CONCLUSION

The decision of the Iowa Supreme Court that the Iowa single sales factor apportionment formula is facially constitutional and constitutional as applied to the net income of Moorman is based upon the constitutional principles so carefully and painstakingly formulated by this Court in a number of cases. To reverse that decision and find either that the Iowa formula is facially invalid or invalid as applied to Moorman would create a constitutional formulary and allow a taxpayer to strike down any formula on the basis of mere assumptions and hypotheticals.

On its face, the Iowa statutory sales formula does not cause extraterritorial taxation, but reasonably apportions net

income to Iowa in conformance with the guarantees of due process.

On its face, the Iowa statutory sales formula does not create multiple taxation and discrimination against interstate commerce in violation of the commerce clause.

On its face, the Iowa statutory sales formula does not violate equal protection, but treats all corporations doing business in Iowa and engaged in selling goods in the Iowa market place alike.

As applied to Moorman's net income, the stipulated record herein does not show that the Iowa formula transgresses any of Moorman's constitutional rights.

In view of the appropriate constitutional principles to be applied in resolution of the instant tax dispute, the viability of the Iowa sales formula cannot be seriously challenged as a constitutional disruption of the United States common market.

The decision of the Iowa Supreme Court should be affirmed and Moorman's appeal dismissed.

Respectfully submitted,

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APPENDIX

APPENDIX A

CONSTITUTION OF THE UNITED STATES

ARTICLE I.

* * *

Section 8. The Congress shall have Power . . .

* * *

To regulate Commerce . . . among the several States . . . ;

AMENDMENT 14.

Section 1. * * *; nor shall any State deprive any person of . . . property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

APPENDIX B

CODE OF IOWA

422.33 Corporate tax imposed

A tax is hereby imposed upon each corporation organized under the laws of this state, and upon every foreign corporation doing business in this state, annually in an amount . . .

1. If the trade or business of the corporation is carried on entirely within the state, the tax shall be imposed on the entire net income, but if such trade or business is carried on partly within and partly without the state, the tax shall be imposed only on the portion of the net income reasonably attributable to the trade or business within the state, said net income

attributable to the state to be determined as follows:

a. Interest, dividends, rents and royalties (less related expenses) received in connection with business in the state shall be allocated to the state, and where received in connection with business outside the state, shall be allocated outside of the state.

b. Net income of the above class having been separately allocated and deducted as above provided, the remainder of the net income of the taxpayer shall be allocated and apportioned as follows:

* * *

Where income is derived from the manufacture or sale of tangible personal property, the part thereof attributable to business within the state shall be in that proportion which the gross sales made within the state bear to the total gross sales.

The gross sales of the corporation within the state shall be taken to be the gross sales from goods delivered within the state, excluding deliveries for transportation out of the state.

For the purpose of this section, the word "sale" shall include exchange, and the word "manufacture" shall include the extraction and recovery of natural resources and all processes of fabricating and curing. The words "tangible personal property" shall be taken to mean corporeal personal property, such as machinery, tools, implements, goods, wares, and merchandise, and shall not be taken to mean money deposits in banks, shares of stock, bonds, notes, credits, or evidence of an interest in property and evidences of debt.

2. If any taxpayer believes that the method of allocation and apportionment hereinbefore prescribed, as administered by the director and applied to his business, has operated or will so

operate as to subject him to taxation on a greater portion of his net income than is reasonably attributable to business or sources within the state, he shall be entitled to file with the director a statement of his objections and of such alternative method of allocation and apportionment as he believes to be proper under the circumstances with such detail and proof and within such time as the director may reasonably prescribe; and if the director shall conclude that the method of allocation and apportionment theretofore employed is in fact inapplicable and inequitable, the director shall redetermine the taxable income by such other method of allocation and apportionment as seems best calculated to assign to the state for taxation the portion of the income reasonably attributable to business and sources within the state; not exceeding, however, the amount which would be arrived at by application of the statutory rules for apportionment.

422.35 Net income of corporation -- how computed.

The term "net income" means the taxable income less the net operating loss deduction, both as properly computed for federal income tax purposes under the Internal Revenue Code of 1954, with the following adjustments:

1. Substract interest and dividends from federal securities.

2. Add interest and dividends from foreign securities and from securities of state and other political subdivisions exempt from federal income tax under the Internal Revenue Code of 1954.

3. Where the net income includes capital gains or losses, or gains or losses from property other than capital assets, and such gains or losses have been determined by using a basis established prior to January 1, 1934, an adjustment may be made, under rules and regulations prescribed by the director, to reflect the difference resulting from the use of a basis of cost or January 1, 1934, fair market value, less depreciation allowed or allowable,

whichever is higher. Provided that the basis shall be fair market value as of January 1, 1955, less depreciation allowed or allowable in the case of property acquired prior to that date if use of a prior basis is declared to be invalid.

4. Subtract fifty percent of the federal income taxes paid or accrued, as the case may be, during the tax year, adjusted by any federal income tax refunds; and add the Iowa income tax deducted in computing said taxable income.

5. Add the amount by which the basis of qualified depreciable property is required to be increased for depreciation purposes under the Internal Revenue Code Admendments Act of 1964 to the extent that such amount equals the net amount of the special deduction allowed on the basis of the amount by which the depreciable basis of such qualified property was required to be reduced for depreciation purposes under the Internal Revenue Code Amendments Act of 1962. The "net amount of the special deduction" shall be computed by taking the sum of the amounts by which the basis of qualified property was required to be decreased for depreciation purposes for the years 1962 and 1963 and subtracting from it the sum of the amounts by which the basis of such property was required to be increased, prior to 1964, for depreciation or disposition purposes under the Internal Revenue Code Amendments Act of 1962.

Provided, however, that a corporation affected by the allocation provisions of section 422.33 shall be permitted to deduct only such portion of the deductions for net operating loss and federal income taxes as is fairly and equitably allocable to Iowa, under rules prescribed by the director.

CERTIFICATE OF SERVICE

I, Harry M. Griger, certify that I served printed copies of the foregoing Brief For The Appellee on the 23rd day of January, 1978, by depositing the same in the United States mails, with first class postage prepaid, addressed to the following named persons at the addresses shown:

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FOR ARGUMENT

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In the Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
STATE OF IOWA,
Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

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REPLY BRIEF FOR THE APPELLANT

The three briefs in opposition among them contain some rewording of old arguments that could be misleading, and even some matters completely irrelevant to the case. We want to ensure that the Court will not be distracted from the sole issue in the case: the unconstitutionality, under the Commerce, Due Process and Equal Protection clauses and a basic principle of federalism, of the Iowa single-sales-factor formula for attributing to Iowa the entire income derived by Moorman Manufacturing Company from manufacturing in Illinois products which it sells to customers located in Iowa. We will try to clarify.

I. BRIEF OF APPELLEE G. D. BAIR

Appellee's brief rests upon repetition of four themes: (1) Iowa didn't tax 100% of the relevant income; (2) taxpayers have such a heavy burden of proof as to preclude review of any formula; (3) "rough approximation" in apportioning income is sufficient; (4) hypotheticals don't prove anything. We can agree with three (3) and four (4) as abstract propositions, but they avail appellee nothing here; while two (2) exaggerates and one (1) is wrong.

(1) Appellee repeats so often the claim that the assessments don't attempt to tax 100% of Moorman's net income derived from goods sold to Iowa customers as to suggest he is merely trying to convince himself of what he knows is not so. The point is not debatable, notwithstanding that the Supreme Court of Iowa stumbled over it when presented, not by the appellee, but by an *amicus*. It is very simple: the statute defines net income, which prescribes the same tax base for all taxpayers, local and foreign. Then the statute attributes to Iowa the amount of that income measured by a fraction, the numerator of which is gross receipts from customers in Iowa and the denominator gross receipts from all customers. The mere statement of the statute itself is sufficient, without more, to establish unequivocally that the assessments aim at 100% of the relevant income. The mathematical proof thereof is shown by Moorman's actual figures in Appendix E to our brief and illustrated by a simplified hypothetical at pp. 27-28 of our brief.

In *General Motors Corporation* v. *District of Columbia*, 380 U.S. 553 (1965), this Court fully recognized that a single-sales-factor formula necessarily taxes 100% of the income from the pertinent segment of the business (at 559):

> "The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which sales are made will allocate 100% of the income to themselves."

The argument (borrowed by the Iowa court) that less than 100% of Moorman's apportionable income was attributed to Iowa ignores the Iowa statutory definition of "net income" and attempts to expand that definition as to Moorman from the amount agreed upon. That effort did not extend to other taxpayers, but to Moorman alone—which does not commend itself as equal protection.

(2) The trial court's findings of fact thoroughly dispose of the burden of proof argument. We begin, as we must, with the underlying assumption that sales to Iowa customers were equally profitable with all other sales—the *statute* makes the assumption, not we, and we do not attack it, as appellee does in complaining that we have not shown by separate accounting that the assumption is valid.

All division of income formulae necessarily rest upon assumptions. As appellee says, a taxpayer has a tough time upsetting those assumptions. The situation here is that we accept the aforesaid assumption upon which the Iowa statute is necessarily based, and our opponents are challenging us—not to overcome, but to prove—the assumption inherent in their statutory formula. We don't have to prove its validity—if the assumption is invalid the statute is invalid. In attacking it, they assert its in-

validity (as to which, of course, they would have the burden of proof). Theirs is the most self-defeating argument imaginable: the Iowa formula doesn't measure income attributable to Iowa and therefore is valid to attribute income to Iowa.

Repudiating its own assumption, Iowa's brief insistently demands separate accounting, such as was used in *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123 (1931) (which was not a unitary business). *Butler Bros.* v. *McColgan*, 315 U.S. 501 (1942) establishes that separate accounting is impermissible for a unitary business such as Moorman. Separate accounting *apportions* nothing; rather it specifically assigns situs to each of *numerous* items of income and expense. Only a *single* item is subject to apportionment, and in the case of the Iowa statute that item is "net income" as defined by the statute.

(3) To be valid, an apportionment formula must reach "a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates." *General Motors Corporation* v. *District of Columbia, supra.* The Iowa formula fails to make such a rough approximation because it does not take cognizance of the locus of either manufacturing labor or capital. This fatal flaw is not present in either a single property formula or a three factor formula, which this Court has approved.

(4) Hypotheticals are not offered to prove anything. The claim (p. 18) that our statement (that the sales factor merely identifies income and does not apportion it) "is a mere economic theory" is wrong on two counts: in the field of taxation constitutional principles embody economic realities; and we didn't merely state it—we demonstrated it mathematically, in a simplified hypothetical in

the text (pp. 27-28) and with Moorman's actual figures in the Stipulation, on pages 12 and 13 of our opening brief, and in Appendix E to our opening brief. Furthermore, this Court has recognized the fact: "the geographic distribution of a corporation's sales is, by itself, of dubious significance in indicating the locus of either" sources of income or social costs. *General Motors Corporation* v. *District of Columbia, supra.*

* * *

The appellee's brief picks up some of the irrelevancies of the brief filed by the Multistate Tax Commission, notably the absence of consideration of Moorman's subsidiaries, none of which, incidentally, had any activities or customers in Iowa. Moorman's apportionable income, the apportionment factors, and the tax rates are all agreed upon, the sole question being whether the sales factor may be employed alone to the complete disregard of all other considerations.

On p. 17 of his brief, appellee asserts that some of the apportionment formulae approved by this Court attributed to the taxing state more income than Iowa's formula would have attributed, followed by the *non sequitur* that therefore the Iowa formula is valid. The assertion is correct when the taxpayer's factory was in the state—*Underwood Typewriter Company* v. *Chamberlain*, 254 U.S. 113 (1920), *Kent-Coffey Mfg. Co.* v. *Maxwell*, 291 U.S. 642 (1934)—while the opposite is true if the local activity was selling—*Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271 (1924), *Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U.S. 450 (1959), *Butler Bros., supra.* Equally irrelevant is the fact that each of these formulae would have attributed less income to Iowa in the facts of this case than would Iowa's.

Relying on *General Motors Corporation* v. *Washington*, 377 U.S. 436 (1964), and *Standard Pressed Steel Co.* v. *Washington*, 419 U.S. 560 (1975), appellee asked at p. 30: "If Iowa . . . could have levied an unapportioned gross income tax upon Moorman . . . why cannot Iowa levy its tax upon a lesser apportioned net amount?" *General Motors Corporation* v. *Washington, supra* and *Standard Pressed Steel Co.* v. *Department of Revenue, supra*, involved gross receipts taxes which, in their nature and incidence, are indistinguishable except semantically from sales and use taxes, generally payable to the state of the user and to no other state. *Gwin, White & Prince* v. *Henneford*, 305 U.S. 434 (1939); *Freeman* v. *Hewit*, 329 U.S. 249 (1946). Presumably, no other state could properly tax Standard Pressed Steel's receipts from Washington customers. Illinois does tax (quite properly) income from goods sold to Iowa customers. Multiple taxation is avoided in the gross receipts tax cases, not by apportionment, but by allowing a single state to impose the entire tax. Since several states are reasonably entitled to tax parts of the net income of a multistate business, apportionment is necessary. Appellee seemingly agrees that apportionment is required in this case, but Iowa presents a formula which does not apportion but seizes the entire relevant income.

Disparities in the amounts of tax induced by varying tax schemes are irrelevant to the validity of any scheme, but since appellee raises the point, we note that had Iowa employed the Washington scheme its tax would have been less than 65% in 1972 and no more than 86% in any year of that demanded by Iowa.

Obviously erroneous is the statement on p. 18 of appellee's brief: ". . . The Iowa sales formula apportions net income to Iowa on the basis of an interstate corporation's business transacted in the Iowa market place—an obvious

income producing activity". Moorman's business in Iowa is transacted at its warehouses and through its salesmen. The fact is that the Iowa formula has no relation to any of the "business transacted" nor to any of the "activity" at all but is governed solely by the location of customers, which clearly is not an income producing factor.

The repeated (e.g., pp. 19, 32-33) argument that Iowa is free to go its own way regardless of what other states do is without merit. That would lead to a conclusion that each state may use a different theory, each selecting the one that gives it the greatest tax yield—with the poor taxpayer subjected to multiple burdens notwithstanding the Constitutional intent to prevent such a result. The clearest statement is in *Bibb* v. *Navajo Freight Lines, Inc.*, 359 U.S. 520 (1959),[1] which, while noting that state safety regulations are almost never disturbed, struck down Illinois' rule requiring curved truck fender flaps, perfectly valid by itself, solely because of its incompatability with the rules of other states requiring straight flaps. *General Motors Corporation* v. *District of Columbia, supra*, makes the same point in a tax matter. Hence the principle: if many states do it one way, and one state does it another way with resulting unreasonable burdens on interstate commerce, the one state's rule is unconstitutional—unless the one state's way is demonstrably superior, which it was not in *Bibb*, and assuredly was not in *General Motors Corporation* and is not here.

Appellee's reliance on the quotation (to the effect that validity of one state's tax does not depend upon another state's), out of context, from *Austin* v. *New Hampshire*, 420 U.S. 656 (1975), is misplaced. In that case this Court held that New Hampshire's income tax was

1. Reaffirmed this term in *Raymond Motor Transportation, Inc.* v. *Rice, Secretary, Wisconsin Department of Transportation*, 46 U.S.L. Week 4109 (U.S. Feb. 21, 1978).

violative of the privilege and immunities guaranty because it applied to nonresidents but not to residents, and that it was not saved by the fact that another state (Maine) might avoid the effect through adjustment of its own income tax.

II. BRIEF AMICI CURIAE OF IOWA MANUFACTURERS ASSOCIATION ET AL.

The principal argument seems to be that this Court either cannot or should not decide this case. The Association's support for that position rests on inverted thinking. The Association quotes from Justice Frankfurter's dissent in *Northwestern States, supra,* without noting that he would not have allowed the states to tax in the absence of Congressional authorization: "the solution to these problems ought not to rest on the self-serving determination of the States of what they are entitled to out of the Nation's resources". 358 U.S. at 477.

The brief starts with a misleading version of the Question Presented, p. 3, in that it assumes a tax cannot be invalid unless it produces a "grossly distorted result", and then implies, contrary to fact, that there is no evidence of such a result in this case. Tax transgression of constitutional bounds can occur in other ways than producing grossly distorted results, although that is a convenient test for the inapplicability to particular facts of a normally valid formula. *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission,* 390 U.S. 317 (1968). In *Austin* v. *New Hampshire, supra,* the tax was invalid although there was, as to the taxpayer, *no* result, distorted or otherwise.

Several of appellee's arguments are repeated: rough approximation; statutory assumption; separate accounting; and gross receipts taxes. We will not repeat the rebuttal.

In presenting the surprising argument that interstate commerce is not involved, the Association quarrels not only with us but with the State since the "apportionment" part of the statute applies *only* to interstate commerce. Most[2] of Moorman's *sales* were from Iowa warehouses, but all its *business* was in interstate commerce. This is a net income tax, not a sales, use or gross receipts tax.

The Association's Summary Argument displays lack of understanding. Holding the Iowa formula invalid would not "overrule" a single prior decision of this Court, and is, in fact, strongly supported by many, from *Underwood* through *Bass, Ratcliff & Gretton, Norfolk & Western, Northwestern States, Kent-Coffey* and *Butler Bros.,* all *supra.*

The claim that the Court is being asked to legislate a formula is not entirely false since the brief of the Multistate Tax Commission urges just that. But neither *party* has advanced such a request and Appellant has been at pains to point out that there is no issue before this Court other than the single, simple question of the constitutionality of the assessments based on the single-sales-factor formula.

We think it is well established that *risk* of multiple taxation of the same income is constitutionally infirm, *J. D. Adams Mfg. Co.* v. *Storen,* 304 U.S. 307 (1938), *Freeman* v. *Hewit, supra, Gwin, White & Prince, supra, Evco* v. *Jones,* 409 U.S. 91 (1972), but also the argument on that point, pp. 35-36, carefully ignores the fact that not only risk, but *actual* double taxation, has been established in this case. Appellee agrees with us that risk alone is sufficient (p. 27 of his brief).

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2. But not all, as they say. Some shipments were from the factory direct to customers (A. 3; our brief p. 4 fn. 2).

At page 39 of its brief, the Association extends its argument about equal protection in a discussion of relative degrees of "scrutiny" which seems to us to offer no help. The fact is that an out-of-state manufacturer selling into Iowa is disadvantaged as compared to an in-state manufacturer selling either in or out of the state. Our brief pp. 32-35.

III. BRIEF AMICI CURIAE OF MULTISTATE TAX COMMISSION ET AL.

Counsel for the Multistate Tax Commission face a difficult dilemma. They would like this Court to endorse their three-factor formula, but they do not want to offend Iowa (as a potential candidate for their Compact) by supporting Moorman's claim for relief. The result is a mixture of inconsistent ideas, some of which could divert attention from the only issue in this case.

The argument tumbles over its internal conflicts: the Iowa formula reasonably apportions net income, but the Iowa formula unconstitutionally discriminates against interstate commerce; although the statute is unconstitutional Moorman is not entitled to relief because Iowa might have used a different tax base. The only part of that argument that makes any sense is that there is an unconstitutional discrimination against interstate commerce.

On page 5 an attempt is made to import one of the issues in *U. S. Steel Corporation* v. *Multistate Tax Commission*, 46 U.S.L. Week 4115 (U.S. Feb. 21, 1978): the extent, if any, to which a taxpayer's liability may be enlarged by attributing to it income which is not its own. There is no excuse for an outsider to attempt to drag that unrelated question into a case in which it does not exist.

The Commission's request that this Court legislate the three-factor formula is completely inappropriate, being unnecessary (and undesirable) for disposition of the case and contrary to the case-by-case adjudication which this Court follows. (It is also surprising in view of the Commission's determined opposition to any such action by Congress.)

The footnote on p. 6 tries once more to confuse base with apportionment. No matter how narrow the definition of base, it must still be "fairly apportioned". The definition applies to all taxpayers alike. So restricted a base as is suggested would have its effect on rate, but not on apportionment.

CONCLUSION

A very simplified summary of appellant's position is:

(1) The Iowa single-sales-factor of attribution does not "apportion" income but merely identifies the total income from the relevant segment of the business, and then attributes 100% of it to Iowa. Its recognized purpose and effect is to subsidize exports and impose a tariff on imports.

(2) Since income "is the product of capital or labor or both combined" Moorman's income from manufacturing goods in Illinois and selling them to Iowa customers cannot be attributed solely to the loci of customers but must be attributed to the activities (including the sales activities in Iowa) which produce the income and incur the social costs.

(3) The sales factor, alone or in conjunction with valid factors, cannot be justified on any economic or fiscal (and hence constitutional) grounds for apportionment of net income; but it may be tolerated as a one-third part of a three-factor formula universally applied.

(4) Since Illinois has properly taxed a substantial portion of the relevant income, Iowa's reaching for 100% thereof causes double taxation in violation of the commerce clause.

(5) Since much of the earning of the relevant income took place in Illinois, Iowa's attempt to tax all of it is reaching outside its jurisdiction in violation of the due process clause, and, more importantly, of the fundamental principle of federalism that a state may not project itself beyond its geographical boundaries.

(6) For reasons earlier stated, the Iowa formula likewise transgresses the equal protection clause.

(7) As discussed in the *amicus* brief of the economists in support of the Jurisdictional Statement, the economic and fiscal consequences of allowing the Iowa decision to stand would be substantially and extensively damaging.

(8) This Court should declare the Iowa single-sales-factor formula constitutionally impermissible. It need do no more to settle this controversy, the parties having agreed upon the consequence of such a holding.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

v.

G. D. BAIR, DIRECTOR OF REVENUE, STATE OF IOWA,
Appellee.

On Appeal from the Supreme Court of the State of Iowa

BRIEF OF THE COMMITTEE ON STATE TAXATION OF THE COUNCIL OF STATE CHAMBERS OF COMMERCE AS AMICUS CURIAE IN SUPPORT OF APPELLANT

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QUESTION PRESENTED

Whether net income tax on corporations imposed by the Code of Iowa, which attributes to Iowa 100% of the income from the sale of goods manufactured without Iowa, but sold within Iowa, so discriminates against interstate commerce as to violate the Commerce Clause and so unfairly apportions the income derived from such activity as to offend due process.

INTEREST OF THE AMICUS

The Committee on State Taxation of the Council of State Chambers of Commerce (COST) consists of over 100 companies which have multi-state operations and derive income from multi-state sources. The members of COST have a vital interest in the uniform apportionment of income among the states and in the prevention of multiple state taxation. COST has long been involved in the study of interstate business transactions and both COST and its members have accumulated a great deal of expertise with respect to interstate taxation. Accordingly, COST believes that it can make a significant contribution to the Court's consideration of this case.

ARGUMENT

1. Iowa imposes an income tax on corporations whose business is carried on partly within and partly without the state. Where a corporation's income is derived from the manufacture or sale of goods both within and without the state, Iowa employs a single "sales-factor formula" under which the corporation's apportionable net income [1] is attributed to Iowa "in that proportion which the gross sales made within the state bear to the total gross sales." Section 422.33(1)(b), Code of Iowa.[2]

Iowa is the only state requiring the division of income on the basis of a single "sales-factor formula" (J.S. App. A, p. A5; J.S. App. B, p. A37). Forty-four [3] of the forty-

[1] Certain income of the corporation, such as interest, dividends, rents, and royalties, is wholly attributed to the state of its geographic source. Section 422.33(1)(a), Code of Iowa. The remainder of the corporation's net income is apportioned.

[2] Sales are attributed to the state of destination, not of origin. Section 422.33(1)(b), Code of Iowa.

[3] Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Hawaii,

five other states (including the District of Columbia) which impose a corporate income tax utilize a three-factor apportionment formula which takes into account the geographical distribution of a corporation's payroll, property and sales.[4]

Iowa's single sales-factor apportionment formula fails to meet the constitutional test of reasonableness. *See, e.g., General Motors Corp.* v. *District of Columbia*, 380 U.S. 553, 560; *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 120-121; *Bass, Ratcliff & Gretton, Ltd.* v. *State Tax Commission*, 266 U.S. 271, 283; *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123, 132. Specifically, it violates the Commerce Clause of the Constitution, Art. 1, § 8, cl. 3, and the Due Process Clause of the Fourteenth Amendment. Iowa's formula violates the Commerce Clause because it leads ineluctably to multiple taxation of foreign corporations doing business in Iowa, and because it inevitably discriminates against interstate commerce by affording local manufacturers a competitive advantage over their foreign rivals. It offends due process by arrogating corporate income to the state out of all proportion to the business activities within the state.

The constitutionality of a single sales-factor formula was discussed in *General Motors Corp.* v. *District of Columbia, supra*, 380 U.S. 553, in which the Court considered such a formula and found it unauthorized by the statute, which allowed taxation of net income "fairly

Idaho, Illinois, Indiana, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Utah, Vermont, Virginia, and Wisconsin.

[4] Colorado also has a two-factor property and sales formula, and Missouri a one-factor sales formula, which are available to taxpayers at their option as alternatives to the three-factor formula. The forty-fifth state, West Virginia, uses a two-factor formula which omits the sales component of the traditional three-factor formula.

attributable" to business activities within the District of Columbia. The Court undertook to review the Court of Appeals' approval of the District's single sales-factor formula because such approval "lends sanction to an apportionment formula seriously at variance with those prevailing in the vast majority of States and creates substantial dangers of multiple taxation" (380 U.S. at 556-557). While not deciding the constitutional question, the Court noted that the reasonableness standard as it had been articulated in the earlier cases lent "little support to the use of an exclusively sales-oriented approach." [5] Noting that an income apportionment formula should approximate "the distribution of either a corporation's sources of income or the social costs which it generates," the Court concluded that "the geographic distribution of a corporation's sales is, by itself, of dubious significance in indicating the locus of either factor" (380 U.S. at 561).[6]

2. Iowa does not challenge the governing principles relied upon by Moorman. Indeed, Iowa does not even attempt to defend the reasonableness of its apportionment formula. Rather, it attacks Moorman's factual case (Motion to Dismiss, pp. 6-7, 10, 13-14), and accuses Moorman of trying to impose upon it a specific three-factor formula, contrary to the accepted principle that "[t]he Constitution is not formulary" (*Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 550). Motion to Dismiss, pp. 7-8, 9.

The latter contention is simply a misstatement. Moorman seeks only to have Iowa's present single sales-factor formula declared unconstitutional (J.S., pp. 4-5,

[5] For a discussion of the constitutional implications of *General Motors*, *see*, Hellerstein, *State Tax Discrimination Against Out-of-Staters*, 30 Nat'l Tax J. 113, 122 (1977).

[6] For a criticism of the sales factor on economic grounds, *see*, Studenski, *The Need For Federal Curbs On State Taxes On Interstate Commerce: An Economist's Viewpoint*, 46 Va. L. Rev. 1121, 1131-33, 1147 (1960); Hartiss, *Economic Aspects Of Interstate Apportionment Of Business Income*, 37 Taxes 327, 362-63 (1959).

"Questions Presented"). Far from having a three-factor formula forced upon it, Iowa has stipulated to such a formula as the basis on which Moorman's Iowa income will be computed if the single sales-factor formula is invalidated. App. 31. Moreover, Moorman amply demonstrated multiple taxation, discrimination against out-of-state businesses and unfair apportionment of income.

3. *Multiple Taxation.* While a state may impose a net income tax on the portion of a foreign corporation's net income earned from, and fairly apportioned to, the taxing state (*Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U.S. 450), it is equally settled that a state may not "impose a tax which discriminates against interstate commerce * * * by subjecting interstate commerce to the burden of 'multiple taxation' * * *." *Id.* at 458; *see also Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 47 U.S. 157; *J.D. Adams Manufacturing Co.* v. *Storen*, 304 U.S. 307. Iowa does not dispute that an apportionment formula which causes multiple taxation of enterprises engaged in interstate commerce violates the Commerce Clause. Rather, Iowa claims that Moorman's evidence regarding double taxation is inadequate because it is based on the allegedly invalid assumption that Iowa taxed 100% of Moorman's income from Iowa sales and on a comparison of the Illinois and Iowa apportionment formulae "in the abstract," which does not consider Moorman's income-producing activities in all states. Motion to Dismiss, pp. 13-15.

Iowa's argument that it did not tax Moorman on 100% of its income from Iowa sales is based on the availability of deductions from gross income in arriving at Iowa net income. This argument would have weight only if the issue were whether Iowa taxed Moorman on 100% of its *gross* income; however, there is no question that the Iowa corporate income tax in question is a *net* income tax. Iowa does not dispute the fact that, once Moorman's

net income from Iowa sales is determined, Iowa's single sales-factor formula assigns 100% of that income to Iowa.

Indeed, a single sales-factor apportionment formula reaches, and is intended to reach, the entire net income connected with sales in the taxing state, even when capital and labor in other jurisdictions have contributed to the earning of such income. This Court recognized in *General Motors* that a single sales-factor apportionment formula results in the attribution of 100% of the income in question to the jurisdiction having such a formula. *General Motors, supra*, 380 U.S. at 557, 560.

A single sales factor apportionment formula, in the context of the general use of three-factor apportionment formulae which take into account the location of a corporation's property and payroll as well as sales (*see supra* p. 3), necessarily results in multiple taxation, because "the States in which the property and payroll of the corporation are located will allocate to themselves 67% of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100% of the income to themselves." *General Motors, supra*, 380 U.S. at 560. Indeed, Iowa itself has admitted that its single sales factor formula results in double taxation. J.S. App. A, p. A6.

Moorman's evidence of the double taxation of its income from Iowa sales presents concrete proof of the double taxation which this Court found in *General Motors* is inherent in a single sales factor apportionment formula. *General Motors, supra*, 380 U.S. at 560. Moorman limited its evidence to Iowa and Illinois because all of Moorman's products sold in Iowa were manufactured in Illinois. App. 24. Having proven conclusively that the interplay of the Iowa and Illinois apportionment formulae would result in the taxation of 141.76% of its 1968 income from Iowa

sales, Moorman had no reason to present evidence regarding the taxation of its other income in states that had no connection with the income producing activities which resulted in the Iowa sales.

4. *Discrimination Against Out-of-State Businesses.* The granting of competitive advantages to local enterprises, which are withheld from foreign corporations, also violates the Commerce Clause. In *Northwestern States Portland Cement Co.* v. *Minnesota, supra*, 358 U.S. at 458, this Court observed that a state may not "impose a tax which discriminates against interstate commerce * * * by providing a direct commercial advantage to local business, *Memphis Steam Laundry* v. *Stone*, 342 U.S. 389 (1952); *Nippert* v. *Richmond*, 327 U.S. 416 (1946) * * *." Again, Iowa does not claim that an apportionment formula which favors local business is permissible under the Commerce Clause; rather it asserts that Moorman's proof on this question consists of " 'hypothetical cases * * * imagined' ", (quoting *United States* v. *Raines*, 362 U.S. 17, 22) and thus that no showing has been made that its formula "subsidizes exports and imposes a tariff on imports." Motion to Dismiss, pp. 6-7, 10, 13.

To the contrary, Moorman has demonstrated that the necessary result of the single sales-factor apportionment formula is to favor Iowa manufacturers which sell their products in Iowa. This is not the "imagined" possibility that the Court disapproved in *Raines;* it is a real advantage to actual enterprises based in the taxing state. The district court observed this precise effect of Iowa's single sales-factor formula (J.S. App. A, p. A38).

> While Moorman's business in Iowa is subjected to the double tax of both Iowa and Illinois, a similarly situated Iowa interstate manufacturer shipping goods, for example, to Illinois would pay taxes only

in Illinois; then on the one-third portion of its business activity there represented by its Illinois sales.

The Court in *General Motors*, *supra*, 380 U.S. at 560, accepted the validity of this type of proof by noting that, while businesses which manufacture in a three-factor jurisdiction and sell in a single sales factor jurisdiction will be subjected to double taxation, "in some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in the three-factor jurisdictions so that only 33% of their incomes will be subject to state taxation."

Iowa's single sales-factor formula affords this commercial advantage to Iowa-based manufacturers, not only in relation to Illinois-based competitors, but over all interstate businesses making sales in Iowa whose plants and payroll are located in any of the forty-five other states that impose a corporate income tax, because all of the other forty-five states utilize property and payroll in their apportionment formulae.[7] *See*, *supra*, p. 3.

5. *Unfair Apportionment of Income.* A state may impose a tax on a foreign corporation doing business within the state, "if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society." *Wisconsin* v. *J. C. Penney Co.*, 311 U.S. 435, 444. That requirement is satisfied "if the tax is fairly apportioned to the commerce carried on within the State." *Ott* v. *Mississippi Valley Barge Line Co.*, 336 U.S.

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[7] This advantage would exist to a lesser extent over such interstate businesses operating in both Iowa and Colorado which elect to use Colorado's alternative two-factor property and sales apportionment formula. The advantage would not exist over inter-state businesses operating in both Iowa and Missouri which elect to use Missouri's alternative single sales-factor apportionment formula. See *supra* p. 3 n. 4.

169, 174; *Northwestern States Portland Cement Co.* v. *Minnesota*, *supra*, 358 U.S. at 452.

For this reason, the Court held in *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission*, 390 U.S. 317, 325, n. 5:

> A State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to "project the taxing power of the state plainly beyond its borders." *Nashville, C. & St. L.R. Co.* v. *Browning*, 310 U.S. 362, 365 (1940). Any formula used must bear a rational relationship, both on its face and in its application, to property values connected with the taxing state. *Fargo* v. *Hart*, 193 U.S. 490, 499-500 (1904) [footnote omitted].

As before, Iowa does not challenge the validity of the constitutional principle that an apportionment formula which taxes income out of all reasonable proportion to the corporation's business activities within the state violates due process. Rather, Iowa claims that an inadequate evidentiary showing of unreasonably disproportionate taxation of income has been made. Motion to Dismiss, p. 13. However, the district court found on the basis of stipulated facts (J.S. App. B, pp. A28-A29):

> Since the largest quantum of capital and labor respecting its [Moorman's] product sold here results from its Illinois relationship, the Iowa apportionment formula fails to reasonably apportion profits traceable to Illinois operations and taxes those activities occurring in Illinois.

In reversing, the Supreme Court of Iowa did not dispute the factual conclusion of the district court that Iowa was taxing Illinois capital and labor contributions to income. Nevertheless, it found that the Iowa single sales-factor formula (J.S. App. C, pp. A78-A79)

> is fairly calculated to assign to Iowa only that portion of the taxpayer's net income reasonably attributable to the trade or business done in Iowa since the taxing power exerted by this statute bears fiscal relation to the protection, opportunities and benefits given by the state.

The formulation by the Supreme Court of Iowa confuses the due process requirement of a nexus sufficient to support the exercise of a state's taxing power[8] (never in dispute here) with the due process requirement that the tax be "fairly apportioned to the commerce carried on within the State." *Ott* v. *Mississippi Valley Barge Line Co., supra,* 336 U.S. at 174. To satisfy the former is not necessarily to meet the latter.

Here, the fact that Iowa taxed 100% of Moorman's net income from Iowa sales even though Illinois manufacturing activities contributed substantially to the production of such income demonstrates beyond any doubt that Iowa's single sales factor apportionment formula arrogates Moorman's income to Iowa out of all proportion to its activities therein, and projects Iowa's taxing power beyond its borders.

6. While the Court has given states a reasonable latitude in the development of apportionment formulae, it should not give approval to Iowa's aberrant sales-factor formula. To do so, as this Court noted in *General Motors, supra,* 380 U.S. at 553, 556-557, "lends sanction to an apportionment formula seriously at variance with those prevailing in the vast majority of states." Conversely, disapproval of Iowa's unique scheme would consolidate the gains toward uniformity of apportionment formulae which *General Motors* materially promoted and would discourage an emerging trend toward parochial and protectionist state taxation of interstate commerce.

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[8] *See, Wisconsin* v. *J. C. Penney Co., supra.*

The use of a three-factor property, payroll and sales apportionment formula by forty-four of the forty-six states with corporate income taxes represents the culmination of a continuing movement toward use of the three-factor formula during this century. While there still are differences among the states in their definitions of "property," "payroll" and "sales," the use of the same three factors in their apportionment formulae is an important step toward complete uniformity of apportionment formulae and thus toward elimination of multiple taxation.

In 1929, the sixteen states with corporate income taxes used eleven different apportionment formulae, the most popular of which were a one-factor formula based on property and a one-factor formula based on sales. By 1953, fifteen formulae were in use, but sixteen of the thirty-five states with corporate income taxes employed the three-factor formula. Special Subcommittee on State Taxation of Interstate Commerce, House Committee on the Judiciary, *State Taxation of Interstate Commerce,* H.R. Rep. No. 1480, 88th Cong., 2d Sess. (Vol. 1) 119 (1964). The movement toward uniformity of factors was further aided by the adoption in 1957 by the National Conference of Commissioners on Uniform State Laws of the Uniform Division of Income for Tax Purposes Act (UDITPA), which provides in § 9 for a three-factor apportionment formula based on property, payroll and sales.[9]

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[9] The Multistate Tax Compact was adopted in response to the enactment by Congress of P.L. 86-272, 73 Stat. 555 (1959) (15 U.S.C. §§ 381-84), and the introduction of H.R. 11798, 89th Cong., 1st Sess. (1965), as the result of the Congressional study of state taxation of interstate commerce mandated by P.L. 86-272. The acknowledged purpose of the Compact was to preempt potential Congressional legislation dealing with protection of interstate commerce from discriminatory taxation. The Compact, whose constitutionality is now at issue in this Court in another appeal, copied UDITPA.

The Multistate Tax Commission created by the Compact has been inconsistent in its support of the equally weighted three-factor

In 1963, shortly before this Court's decision in *General Motors*, twenty-six of the thirty-eight states with corporate income taxes used the three-factor formula, and the number of different formulae in use had declined to eleven. *State Taxation of Interstate Commerce*, *supra*, at 119. As noted above, this Court's disapproval of the single sales-factor formula in *General Motors* in 1965 further accelerated that trend, so that today forty-four of the forty-six states taxing corporate income use the three-factor formula.

Iowa's single sales-factor apportionment formula is a glaring exception to this trend. However, beginning in 1971, four states which utilize three-factor apportionment formulae—Florida, Wisconsin, New York and Massachusetts—have moved in the direction of Iowa's discrimination against out-of-state businesses by attributing double weight to the sales factor of the apportionment formula, a practice which incorporates to a lesser degree the vice of Iowa's single sales-factor formula.[10] The Court's disapproval of Iowa's formula would discourage this emerging trend away from the generally accepted three-factor formula and thus would solidify the gains that have been made toward uniformity of apportionment and reduction in multiple taxation.

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formula required by UDITPA. For example, Florida, one of the seven founding members, was continued by the Commission as a full member of the Compact notwithstanding that state's adoption of a discriminatory double-weighted sales factor which violated the specific terms of the Compact. Moreover, the Multistate Tax Commission has promulgated regulations which obliterate key elements of UDITPA, particularly with respect to non-business income and the so-called unitary business-combined return concept.

[10] In addition, a bill providing for double weighting of the sales factor was introduced in the Illinois State Senate on April 7, 1977. The bill, S.B. 737, came up for a final vote by the Senate on May 26, 1977, but was recommitted to the Senate Revenue Committee for further study of its revenue impact.

CONCLUSION

For the foregoing reasons, the judgment of the Supreme Court of Iowa should be reversed.

Respectfully submitted,

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ON APPEAL FROM THE SUPREME COURT OF THE STATE OF IOWA

AMICUS CURIAE BRIEF OF THE MULTISTATE TAX COMMISSION AND ATTORNEY GENERAL of the STATE OF OREGON

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IN THE

Supreme Court of the United States

October Term, 1977

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant

v.

G. D. BAIR, Director of Revenue, State of Iowa,
Appellee.

ON APPEAL FROM THE SUPREME COURT
OF THE STATE OF IOWA

AMICUS CURIAE BRIEF OF THE MULTISTATE TAX COMMISSION AND ATTORNEY GENERAL of the STATE OF OREGON

I

STATEMENT OF INTEREST

The Multistate Tax Commission (hereinafter referred to as the Commission) is the official administrative agency of the Multistate Tax Compact (hereinafter referred to as the Compact) entered into cur-

rently by 19 states as full members, and by 13 states as associate members.[1]

The purposes of the Compact are to:

1. Facilitate proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.

2. Promote uniformity or compatibility in significant components of tax systems.

3. Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.

4. Avoid duplicate taxation.

In fulfillment of these objectives in the area of State income taxation of multistate businesses, Article IV of the Compact sets forth the provisions of the Uniform Division of Income for Tax Purposes Act (UDITPA) promulgated by the National Conference of Commissioners on Uniform State Laws in 1957 for the allocation and apportionment of income.[2] It apportions "business income" in accordance with the well recognized three factor apportionment formula of property, payroll, and sales, commented on by this

[1] The current regular members are the states of Alaska, Arkansas, California, Colorado, Hawaii, Idaho, Kansas, Michigan, Missouri, Montana, Nebraska, New Mexico, Nevada, North Dakota, Oregon, South Dakota, Texas, Utah and Washington.

The current associate members are the states of Alabama, Arizona, Georgia, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, Ohio, Oklahoma, Pennsylvania, Tennessee, and West Virginia.

[2] Uniform Laws Annotated, Vol. 9a, p. 448 et seq.

Court in *General Motors Corporation vs. District of Columbia,* 380 U.S. 553 (1965).

Article VII permits the Commission to promulgate advisory rules and regulations concerning this Uniform Act. The Compact also provides Joint audits at the request of member states to further implement uniform enforcement of the Uniform Act. In this manner, the Compact and the Commission have sought to substantially diminish potential problems of overtaxation or undertaxation of the income of enterprises carrying on business activities in two or more states or countries. The Commission is thus concerned with the purpose for, the operative effect of, and the constitutional validity of any state income tax apportionment formula that substantially deviates from the generally accepted and well recognized UDITPA formula contained in Article IV of the Compact and generally utilized by most of the income tax states for the division of income. The Attorney General of the State of Oregon has a comparable concern inasmuch as Oregon is a member of the Compact and has adopted UDITPA for Oregon income tax purposes.

II

ARGUMENT

A. Introductory Considerations.

This is undoubtedly one of the most important cases this Court has been asked to decide pertaining to the constitutional limitations on a state's power to tax the income of multistate-multinational corporations. The primary purpose of this brief is to place the

issue in this cause in what we believe to be its proper constitutional setting and to suggest a resolution of that issue. While the Appellant and Appellee will undoubtedly argue that resolution of this case is controlled by precedent, we believe that if this Court is to decide that the single-sales-factor apportionment formula is unconstitutional, it is necessary that the interstate commerce and due process clauses limitations on state taxing power be applied in a different manner than has heretofore been the case.

The issue in this cause is whether or not the Iowa single-sales-factor apportionment formula is unconstitutional on its face or as applied to Appellant because it attributes the income of an integrated manufacturing-sales corporation, which is subject to apportionment under Iowa law, to the distribution of sales rather than to the distribution of tangible property, payroll, and sales. Inasmuch as the record contains no evidence that the Iowa formula arrives at an unreasonable result or taxes extra-territorial income of the Appellant except for the fact that the formula attributes no income to the manufacturing activities of Appellant in Illinois and except for the fact that Illinois apportions income for income tax purposes by the well-recognized three-factor apportionment formula (property, payroll, and sales), the constitutionality of the single-sales-factor apportionment formula as applied really turns on whether or not it is unconstitutional on its face. This is a question of first impression.

Resolution of the constitutionality of the Iowa formula as applied in this case is compounded by the fact that Iowa did not subject to tax all of the net income of the Appellant and by the further fact that not all of the net income of the Appellant which was subject to tax was apportioned. Some of Appellant's net income was specifically allocated without a determination of whether or not it was part of Appellant's unitary income and therefore part of apportionable income for constitutional limitation purposes. Furthermore, the Appellant carried on some of its business activities through subsidiary corporations and there is nothing in the record to indicate that Appellant was not carrying on an integrated unitary business with such corporations. If it did carry on a unitary business with its subsidiary corporations, the constitutionality of the Iowa formula should be determined in reference to the total unitary income of Appellant and its subsidiary corporations and not just the income of Appellant.

Inasmuch as the states are entitled to a reasonable apportionment of all unitary income of a unitary business (whether carried on in a single or multiple corporate form), in addressing the question of the constitutionality of Iowa's single-sales-factor apportionment formula, this Court should clearly indicate in any decision in this cause that it has reference to the total unitary income of a unitary business and *not*

the particular income of Appellant subject to apportionment by Iowa.[3]

If multistate-multinational businesses are required to pay their fair share of state taxation free from discriminatory or multiple tax burdens, we believe this case poses the following issue for resolution:

> Whether or not the due process and commerce clause restrictions for state income tax purposes preclude a state from apportioning unitary income of a unitary enterprise conducting integrated manufacturing-sales operations by an apportionment formula which deviates from the generally accepted and well-recognized equally weighted "three-factor formula" of payroll, property, and sales (UDITPA) in the absence of any showing by the state or the taxpayer that this formula arrives at an unreasonable result.

While we realize that resolution of this issue requires this Court to take a different approach in resolving state income tax apportionment disputes, we believe it is the basic issue in this cause since the apportionment result of the Iowa single-factor formula is challenged by the Appellant because it deviates from the three-factor formula and thereby allegedly results in subjecting the Appellant to multiple and discriminatory taxation by Iowa.

We believe that if this Court does not adopt a

[3] For example, if Iowa subjected only one-third of the entire unitary net income to tax and apportioned that on the basis of a single-sales-factor apportionment formula, the result would be no different in practical operation and effect than if it applied the property, payroll and sales factors apportionment formula to the entire unitary income. Appellant is thus in error in arguing (Jur. St., p. 3) that what constitutes a state's apportionable income tax base is irrelevant in deciding the constitutionality of an apportionment formula.

standard against which to test the validity of the Iowa apportionment formula, it has no basis for invalidating that formula. Furthermore, simply invalidating the single-sales Iowa apportionment formula still leaves multistate-multinational businesses exposed to multiple and discriminatory taxation by the states by other comparable formulae. Inasmuch as the property, payroll, and sales fairly and adequately measures the major income producing components of general commercial enterprises, there is no reason why these components, equally weighed, should not constitute an appropriate and presumably valid apportionment standard to measure the constitutionality of state income tax apportionment formulae as applied to the unitary income of integrated manufacturing-sales businesses within the purview of the commerce and the due process restrictions of the federal constitution.

The purpose of this brief is to indicate why we believe this to be so and why we believe it is required if the constitutional limitations on state taxing power as developed by this Court are to be placed in practical operation and effect.

B. The Results of Prior Apportionment Cases of This Court, Which Have Prescribed No Apportionment Standard to Resolve the Reasonableness of or Discriminatory Effect of any State Income Tax Apportionment Formula, Support the Decision of the Iowa Supreme Court.

The Supreme Court of Iowa upheld the single-

sales-factor apportionment formula on its face and as applied to Appellant because it

> " . . . is fairly calculated to assign to Iowa only that portion of the taxpayer's net income reasonably attributable to the trade or business done in Iowa since the taxing power asserted by this statute bears fiscal relation to the protection, opportunities and benefits given by the State." (Jur. St. A78-A79).

and because

> "Under the record, Moorman has not carried its burden, since it has not demonstrated by the stipulated facts the Iowa single-sales-factor apportionment formula constitutes an unreasonable and arbitrary application in Moorman's particular case. (A87 Jur. St.)

In determining whether or not the Iowa Supreme Court arrived at a proper conclusion in light of prior decisions of this Court, we note the following due process and commerce clause principles:

1. The States may determine their share of the unitary income of a unitary business by an apportionment formula. *Northwestern Cement Co. v. Minnesota*, 358 U.S. 450 (1959); *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920); *Bass, Ratcliffe & Gretton, Ltd. v. State Tax Commission*, 266 U.S. 271 (1924); *Butler Bros. v. McColgan*, 315 U.S. 501 (1942); *General Motors Corp. v. District of Columbia*, 380 U.S. 553 (1965).

2. Single factor apportionment formulae are not *per se* unconstitutional. *Underwood Typewriter Co. v. Chamberlain, supra; Bass, Ratcliffe & Gretton, Ltd. v. State Tax Commission, supra; National Leather Co. v. Massachusetts*, 277 U.S. 413 (1928); *Maxwell v. Kent-Coffey Mfg. Co.* 264 N.C. 365, 168 S.E. 397 (1933) aff'd 291 U.S. 642 (1933); *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939); and *General Motors Corp. v. District of Columbia, supra.*

3. It is impossible for a state to achieve a perfect apportionment of expansive complex business activities and rough approximation rather than precision is sufficient. *International Harvester v. Evatt*, 329 U.S. 416 (1947).

4. A taxpayer challenging the result reached by the application of an apportionment formula has a heavy burden and must establish by "clear and cogent evidence" that the apportionment formula results in the taxation of extraterritorial values. *Butler Bros. v. McColgan*, 315 U.S. 501, 507 (1942); *Norfolk & Western R. Co. v. North Carolina*, 297 U.S. 682, 688 (1936); and *Norfolk & W. R. Co. v. Tax Commission*, 390 U.S. 317, 326 (1968).

5 A tax on "interstate commerce" must be fairly apportioned to the commerce carried on within the state. *Ott v. Mississippi Valley Barge Line Co.*, 336 U.S. 169, 174 (1949); *Complete Auto Transit v. Brady*, 430 U.S. 274, 279 (1977); *Northwestern Cement Co. v. Minnesota, supra*, 358 U.S. 460 (1959).

In applying the foregoing principles, to our knowledge this Court has never declared a state apportionment formula invalid under the Constitution by reference to a more rational or reasonable apportionment formula. Furthermore, to our knowledge, it has never de-

clared an apportionment formula invalid on its face, or decided an apportionment case by reference to its discriminatory or multiple burden effect on interstate commerce.[4]

Underwood Typewriter Co. v. Chamberlain, supra, upheld a single-factor-property formula apportioning net income to Connecticut against due process and commerce clause attack. This is so even though this Court there noted that the profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut and ending with sales in other states. Likewise *Maxwell v. Kent-Coffey Mfg. Co., supra,* 204 N.C. 365, 168 S.E. 397 (1973) aff'd *per curiam* 291 U.S. 624 (1933) upheld a single-factor-property formula which attributed 99 % of the net income of a corporation to North Carolina even though the corporation sold less than 1% of its products in North Carolina. In *Ford Motor Co. v. Beauchamp, supra,* 308 U.S. 331 (1939), this Court upheld a single-factor gross receipts apportionment formula in apportioning capital to Texas for Texas corporate franchise tax purposes. The validity of such apportionment formulae is no more or less constitutionally suspect than the Iowa single-sales-factor apportionment formula.

In order to invalidate an apportionment formula, taxpayers have been required to resort to "separate

[4] As indicated by argument under the subdivision of this brief beginning on page 18, we believe the Iowa single-sales-factor apportionment formula is invalid on its face because it discriminates against out-of-state manufacturers and interstate commerce if some income is constitutionally required to be attributed to manufacturing.

accounting". In *Hans Rees Sons, Inc. v. North Carolina,* 283 U.S. 123 (1931), the taxpayer was able to establish by the proffer of evidence that its "manufacturing profit" represented only 17% of its profit while the North Carolina property factor apportioned 66% to 85% of the profit to North Carolina. Based upon this proffered evidence, this Court found the North Carolina property factor unconstitutional as applied. Similarly, In *Norfolk & Western Railway Co. v. Missouri State Tax Commission,* 390 U.S. 317 (1968), this Court invalidated the application of an ad valorem property tax apportionment formula which attributed $20,000,000 of rolling stock to the state where the taxpayer demonstrated that only $7,600,000 of its rolling stock was in the state.

Consistent with the results reached by this Court in its prior decisions, there is no basis for concluding that the single-sales-factor apportionment formula of Iowa facially or as applied to Appellant is unconstitutional because it does not result in a rough approximation of the net income reasonably attributable to Iowa sources. These decisions recognize that it is impossible to determine what portion of the net income of a unitary integrated enterprise can be attributable to specific properties, activities or sources of such an enterprise; that rough approximation is all that is required of an apportionment formula; and that the taxpayer has the burden of establishing by "clear and cogent" evidence that an apportionment formula has the practical effect of taxing extraterritorial values.

Tested against these standards, we believe there is nothing in the record in this cause that indicates that the Iowa single-sales-factor apportionment formula has taxed net income of Appellant not reasonably attributable to Iowa sources. States otherwise, for example, there is nothing in the record to establish that the warehousing and selling in Iowa of approximately 22% ($22,102,015) of the total products sold by Appellant for the fiscal year ending March 31, 1968, did not increase Appellant's net income for that period by the amount of $1,548,284 out of a total taxable income prior to Iowa adjustments of $10,393,161 without consideration of the effect of and whether or not Appellant conducted a unitary business with its subsidiary corporations.[5] If the Appellant could not have used Iowa as a market for 22% of its products, it may well have realized no net income for the year ending March 31, 1968. This is exemplified by the current plight of the United States Steel industry due to foreign competition for American steel markets. Furthermore, it is no more unreasonable to attribute all of the profits of Appellant to sales than it is to attribute it to tangible property.

Thus, if the due process and commerce restrictions on state taxing power as applied to interstate commerce *only* require that a state's apportionment formula arrive at a rough approximation of income attributable to instate sources; that it be reasonably related to the benefits conferred by the taxing state; and that the burden is on the taxpayer to establish the contrary by "clear and cogent" evidence; we believe the Iowa Supreme Court arrived at a proper result in this case based on the single factor apportionment cases such as *Underwood Typewriter Co. vs. Chamberlain supra,* and *Ford Motor Co. v. Beauchamp, supra.* The Appellant has not established by "clear and cogent" evidence that the apportionment result attributed more of its net taxable income to Iowa than reasonably attributable to Iowa sources particularly in the *absence of a controlling constitutional standard for determining a fair or rational apportionment.* Appellant *assumed* that the three-factor formula was the constitutional standard and from that premise argues the unconstitutionality of the apportionment result.

[5] If Appellant actually carried on a unitary business with its subsidiaries, net income of that business and the apportionment result of applying the Iowa single-sales-factor apportionment formula to the net income of such a unitary business is not known.

C. *In Order to Require Multistate-Multinational Businesses to Pay Their Fair Share of State Income Taxes and to Protect Such Businesses From Discriminatory or Multiple State Income Taxes, It Is Necessary That This Court Prescribe a Rational and Fair Apportionment Standard for the Apportionment of State Income Taxes.*

This Court has consistently interpreted the commerce clause as freeing interstate commerce from undue or multiple tax burdens and from discriminatory taxation as compared to intrastate commerce. *Northwestern Cement Co. v. Minnesota, supra; Complete Auto Transit v. Brady, supra; General Motors Corp.*

v. Washington, 377 U.S. 436 (1964). In order to relieve interstate commerce from such burdens or discrimination, it has required the use of apportionment formulae designed to tax only that portion of an interstate business carried on within a taxing state, *Central Greyhound Lines v. Mealey*, 334 U.S. 653 (1948), and required apportionment formulae to bear a rational relationship to activities and properties within a taxing state, *Norfolk v. Western Railway Co. v. Missouri*, 390 U. S. 317 (1968) and to be fairly apportioned (*Complete Auto Transit, Inc. v. Brady, supra; General Motors v. District of Columbia, supra.*)

However, by not defining what constitutes a rational or fair apportionment, this Court has left the states free to choose their own apportionment formulae subject to the rough approximation and "clear and cogent" evidence standards. As a practical matter, then, the states, by the application of different apportionment formulae, may, within the framework of the decided apportionment cases, subject interstate commerce to multiple burdens and may in fact design apportionment formulae which in practical operation and effect, when considered together with other apportionment formulae, discriminate against "interstate" commerce as compared to "intrastate" commerce. This the commerce clause was never designed to permit [6].

[6] The following statements from *Northwestern Cement Co. v. Minnesota, supra*, appear to state the position this Court has taken with regard to the multiple burden-discrimination issue under the commerce clause:

"While the economic wisdom of state net income taxes is one of

The need for a rational standard to resolve multiple burden and discrimination problems is not alleviated by simply holding that the Iowa single-sales-factor formula is unconstitutional because it does not constitute a fair or rational apportionment formula. Iowa could comply with such a holding by giving limited weight to the out-of-state activiites of the Appellant. This could still leave the Iowa formula at substantial variance with the equally weighted three-factor apportionment formula of property, payroll and sales. This Court in striking down the single-sales-factor ap-

state policy not for our decision, one of the 'realities' raised by the parties is the possibility of a multiple burden resulting from the exactions in question. The answer is that none is shown to exist here. This is not an unapportioned tax which by its very nature makes interstate commerce bear more than its fair share. As was said in *Central Greyhound Lines v. Mealy*, 334 U.S. 653, 661 (1948), ' . . . it is interstate commerce which the State is seeking to reach and . . . the real question [is] whether what the State is exacting is a constitutionally fair demand by the State for that aspect of the interstate commerce to which the State bears a special relation.' The apportioned tax is designed to meet this very requirement and 'to prevent the levying of such taxes as will discriminate against or prohibit the interstate activities or will place the interstate commerce at a disadvantage relative to local commerce.' *Id.* at 670. Logically it is impossible when the tax is fairly apportioned, to have the same income taxed twice. In practical operation, however, apportionment formulas being what they are, the possibility of the contrary is not foreclosed, especially by levies in domiciliary States. (footnote omitted) But that question is not before us. It was argued in *Northwest Airlines v. Minnesota*, 322 U.S. 292 (1944), that the taxation of the entire fleet of its airplanes in that State would result in multiple taxation since other States levied taxes on some proportion of the full value thereof. The Court rejected this contention as being 'not now before us' even though other States actually collected property taxes for the same year from Northwest upon 'some proportion' of the full value of its fleet. (footnote omitted) Here the records are all to the contrary. There is nothing to show that multiple taxation is present. We cannot deal in abstractions. In this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense. This they have failed to do." (358 U.S. 450 at pp. 462-463).

portionment formula in *General Motors v. District of Columbia, supra,* leaves the District formula in the same posture.

What we are suggesting is that if Interstate commerce is required to pay its fair share of state income taxes without being subject to discriminatory or multiple taxation (without congressional intervention) the traditional role of this Court in the disposition of income tax apportionment disputes requires modification. A greater degree of uniformity will be required to achieve these constitutional objectives than can be achieved by determining the constitutionality of a particular apportionment formula in the absence of a practical constitutional standard prescribed by this Court. In the absence of such a standard, how can a multiple taxation question or a tax discrimination question be resolved? Given the vagaries of the elements which produce the "net income" of modern complex businesses, how can this Court determine whether a particular apportionment formula results in a "fair" or "rational" apportionment, unless an apportionment formula is "tested" by reference to a standard deemed to be fair and rational by this Court?

In the instant case, the Appellant claims it is subject to multiple and discriminatory taxation on its Iowa business as a result of interaction of the Iowa single-sales-factor apportionment formula and the Illinois three-factor apportionment formula. If this results in unconstitutional multiple or discriminina-

tory taxation, is Iowa's formula invalid or is the formula of Illinois invalid? This can only be resolved by determining which formula more rationally and fairly apportions income. This Court cannot logically declare Iowa's single-sales-factor apportionment formula unconstitutional without negatively or affirmatively determining that another apportionment formula prescribes the constitutional limit which Iowa cannot exceed. Neither do we believe that it can, without the application of a standard, determine that the Iowa formula, standing alone, is not reasonably related to the income produced and the activities of Appellant in the state of Iowa for the years in question.

Net income is an abstract concept resulting from a host of operational events and transactions which take place within a time frame called a "tax year", all of which are significant in producing net income. In integrated commercial operations, net income is a product of labor, capital and sales. Without all of these major components, it is highly unlikely that any net income could be produced. Absent any standard, it is not unreasonable to attribute all net income to the distribution of property (*Underwood Typewriter Co. v. Chamberlain, supra*). Since there is no reason to assume that property is more important than sales in the production of net income, *Underwood* supports the constitutionality of the Iowa single-sales-factor apportionment formula as resulting in fair apportionment of unitary income.

We therefore respectfully submit that this Court

should conclude that the generally accepted, equally weighted three-factor apportionment formula of property, payroll and sales (UDITPA) constitutes the constitutional standard for state income tax apportionment purposes as applied to the total unitary income of integrated manufacturing-selling businesses; and that it is controlling for the apportionment of the total unitary income of such businesses unless the state or taxpayer establishes by clear and cogent evidence that its particular application produces an unreasonable result.

If, as noted by this Court in *General Motors v. District of Columbia, supra,* the standard three-factor formula is utilized by a great majority of the income tax states and it "can be justified as a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates" (380 U.S. 561), it represents a reasonable and logical presumptive controlling constitutional standard for the apportionment of a general business corporation's unitary income. In the absence of adopting this or some other constitutional standard to determine the reasonableness of a state income tax apportionment formula, we do not believe it is appropriate for this Court to declare the Iowa single-sales-factor apportionment formula invalid because it assigns to Iowa an unconstitutional portion of net income.

D. Even Though Iowa's Single-Sales-Factor Apportionment Formula, Consistent With Prior Apportionment Decisions of This Court, Reasonably Apportions Net Income to Iowa, It Unconstitutionally Discriminates Against Out-of-State Manufacturers-Sellers If the Constitutionality of Such Formula Is Tested Against the Standard Three-Factor Formula or Any Other Formula Which Assigns Some Income to Manufacturing.

This Court has consistently held that the fundamental purpose of the commerce clause was to protect interstate commerce from discriminatory regulation or taxation. *Baldwin v. G.A.F. Seelig, Inc.,* 294 U.S. 511 (1935); *Guy v. Baltimore,* 100 U.S. (10 Otto) 434 (1880); *Darnell & Son v. Memphis,* 208 U.S. 113 (1908); *Northwestern States Portland Cement Co. v. Minnesota, supra; Memphis Steam Laundry v. Stone,* 342 U.S. 389 (1952); *Nippert v. Richmond,* 327 U.S. 416 (1946); *Boston Stock Exchange, et al v. State Tax Commission,* 429 U.S. 318 (1977); *Halliburton Oil Well Co. v. Reily,* 373 U.S. 64 (1963); *Webber v. Virginia,* 103 U.S. 344 (1880); *Walling v. Michigan,* 116 U.S. 446 (1886); *Walton v. Missouri,* 91 U.S. 275 (1875); *Henneford v. Silas-Mason Co.,* 300 U.S. 577 (1937).

As noted by this Court in *Baldwin, supra,* in striking down New York's attempt to regulate the price of out-of-state milk purchases:

> "Neither the power to tax nor the police power may be used by the State of destination with the aim and effect of establishing an economic barrier against competition with the products of another state or the labor of its residents. Restrictions so contrived are an unreasonable clog upon

> the mobility of commerce. They set up what is equivalent to a rampart of customs duties designed to neutralize advantages belonging to the place of origin. They are thus hostile in conception as well as burdensome in result."
> (294 U.S. 527).

As noted by this Court in the *Boston Stock Exchange* case, *supra*:

> "No State may, consistent with the Commerce Clause, 'impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business' [cases cited]. The prohibition against discriminatory treatment of interstate commerce follows inexorably from the basic purpose of the Clause. Permitting the individual States to enact laws that favor local enterprise at the expense of out-of-state businesses 'would invite a multiplication of preferential trade areas destructive' of the free trade which the Clause protects. *Dean Milk Co. v. Madison*, 340 U.S. 349, 356 (1951); (The first quote of the Court is from *Northwestern States Portland Cement Co. v. Minnesota, supra*) (429 U.S. 329).

The discrimination cases under the commerce clause do not rest on due process considerations. Even though the Iowa income tax is reasonably measured by a single-sales-factor apportionment formula and reaches only legitimate taxable in-state activities or sources, if, in practical operation and effect, it permits Iowa to "discriminatorily tax the products manufactured or the business operations performed in any other State" (*Boston Stock Exchange v. State Tax Commission, supra*, 429 U.S. 318, 337), it should be struck down as violative of the commerce clause.

While there can be no question that the commerce clause requires equal tax treatment of interstate commerce as compared to intrastate commerce (*Halliburton Oil Well Co. v. Reily, supra*, and that the practical operation and effect of a state tax system controls in determining the presence or absence of such equality (*Best & Co. v. Maxwell*, 311 U.S. 454 (1940), resolution of discrimination questions depends upon the comparatives used in determining equality.

In *Halliburton, supra*, this Court required "equal treatment for in-state and out-of-state taxpayers similarly situated." (373 U.S. 70). The Iowa statute standing alone treats Appellant and other out-of-state manufacturers-sellers the same as in-state manufacturers-sellers. Both pay an Iowa income tax on Iowa income attributable to Iowa sales.[7] The question of discrimination resolves itself down to a question of the proper *measure* of the Iowa income tax. It is measured by Iowa sales as compared to total sales. If it is permissible to attribute all income of a manufacturer-seller on the basis of the distribution of sales, there is no basis for any claim of discrimination. On the other hand, if some income is required to be assigned to manufacturing, the Iowa formula discriminates against out-of-state manufacturers-sellers selling in Iowa as compared to Iowa manufacturers-sellers selling into other states.

Since the Iowa corporate income tax is imposed

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[7] Since the income of intrastate businesses that manufacture and sell only in Iowa is not apportioned, they pay Iowa income tax on their entire income. Thus, exclusively intrastate business is not favored by the Iowa apportionment formula.

"on the portion of the net income reasonably attributable to the trade or business within the state"; including income derived from the manufacture or sale of tangible personal property (Jur. St., Appendix E, A100), it appears the tax is imposed on both manufacturing and selling. It is an income tax on corporate businesses and not on corporate sales. Therefore, a proper comparison for discrimination purposes may be to compare the practical operation and effect of the Iowa income tax single-sales-factor apportionment formula on instate manufacturers selling out-of-state with out-of-state manufacturers selling in-state.

As indicated by this Court in *General Motors v. District of Columbia, supra*, the single-sales-factor apportionment formula permits an in-state manufacturer that sells its product entirely without the state to pay no tax on income derived from its manufacturing operations and to pay a tax on only a third of its income derived from sales to the states which apportion income by the three-factor formula. On the other hand, an out-of-state manufacturer under the same circumstances would be exposed to a potential tax liability of 167% of its income if it manufactured in a three-factor apportionment state and sold its total product to Iowa. Certainly, this practical operation and effect of the single-sales-factor formula of Iowa coupled with the general use of the three-factor apportionment formula subjects in-state manufacturers to preferential taxation and requires businesses to locate in Iowa or suffer discriminatory taxation.

It is thus evident, however, that if the Iowa single-sales-factor apportionment formula discriminates against in-state manufacturers selling out-of-state as compared to out-of-state manufacturers selling in Iowa, the constitutionality of the Iowa apportionment formula must be determined by reference to what constitutes a "fair" or "rational" apportionment of income to Iowa by reference to the foregoing classification of taxpayers. Since a "fair" and "rational" apportionment is achieved by UDITPA, we believe that this Court should adopt UDITPA as the constitutional standard to resolve multiple or discriminatory tax burden questions under the commerce clause. Without the adoption of this standard or some other standard requiring some income to be apportioned to manufacturing, we do not believe the Iowa formula unconstitutionally discriminates against or imposes a prohibited multiple burden on interstate commerce.

III

CONCLUSION

Historically, this Court has decided apportionment controversies by determining on a case by case basis whether a particular formula of a particular state exceeded constitutional limits. It has never before been confronted with a case where two apportionment formulae, as applied by two states, has the result of subjecting the net income of a taxpayer attributable to the two states to multiple and discriminatory bur-

dens.[8] If both states are to be treated fairly and if interstate commerce is to be freed from such burdens, this Court is required to determine what constitutes a fair and rational apportionment formula for the attribution of the unitary income of a unitary business for state income tax purposes. The Commission believes that the UDITPA three-factor formula which has been adopted by a vast majority of the income tax states and is contained in article IV of the Compact should be determined by this Court to constitute the presumptive constitutional standard for the apportionment of unitary income of an integrated manufacturer-seller business and that such standard should be applied in the instant case to determine whether or not Iowa exceeded that standard by the single-sales-factor apportionment on its face or as applied to the Appellant.

Although we believe resolution of the issue in this case requires the Court to "test" the constitutional validity of the Iowa single-sales-factor apportionment formula on its face against the reasonableness of the three-factor apportionment formula, we do not believe that resolution of this issue would entitle the Appellant to any relief. As noted *supra* at page 5 Iowa has not attempted to apportion the entire unitary income of Appellant and the record does not disclose this entire unitary income and the apportionment results of a three-factor formula applied to this

8 This leads one to believe that maybe the real issue in this case is: "Does one state have to take into account the apportionment formulae of all other states in adopting a formula for apportioning the income of a multistate unitary enterprise?"

unitary income if the Appellant conducted a unitary business with its wholly owned subsidiaries. Under such circumstances, it is not possible to determine whether or not the Iowa formula as applied exceeds the constitutional limit of the apportionment of Appellant's entire unitary income by the three-factor formula.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1977.

No. 77-454

MOORMAN MANUFACTURING COMPANY,
Appellant,

vs.

G. D. BAIR, DIRECTOR OF REVENUE,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF IOWA.

BRIEF AMICI CURIAE OF IOWA MANUFACTURERS ASSOCIATION, DEERE & CO., E. I. DuPONT DeNEMOURS & COMPANY, THE MAYTAG COMPANY, MONSANTO COMPANY, AND STANDARD BRANDS INCORPORATED.

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OPINIONS BELOW.

The opinions and judgment from which this appeal is taken are reported at 254 N. W. 2d 737 (Iowa 1977), and are reproduced in the Appendix at A-103. The opinion of the Iowa Director of Revenue may be found in the Appendix at A-2. The opinions of the Iowa District Court for Polk County are unreported and are to be found in the Appendix at A-56.

JURISDICTION.

This Court's jurisdiction is invoked pursuant to 28 U. S. C. § 1257(2).

CONSENTS OF PARTIES.

Both parties have consented in writing to the filing of this brief *amici curiae* and their letters of consent have been filed with the Clerk of the Court.

INTERESTS OF AMICI CURIAE.

The Iowa Manufacturers Association, organized in 1903, has a membership of 680 manufacturers of both Iowa and non-Iowa origins. The individual corporate *amici* are all heavily engaged in interstate commerce, do substantial business in Iowa, and are subject to the Iowa income tax that is the object of attack in this law suit. All of the members of the Association and the individual corporations would be seriously affected by a decision that the Iowa income tax law was invalid on its face, but are not likely to be affected by any decision on the question whether the statute was invalidly aplied to the Appellant here.

CONSTITUTIONAL AND STATUTORY PROVISIONS.

Article I, § 8, cl. 3 of the Constitution provides:

> The Congress shall have Power . . .To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes;

Amendment XIV, § 1 of the Constitution provides:

> . . . No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United State; nor shall any State deprive any person of life, liberty, or property, without due proces of law; nor deny to any person within its jurisdiction the equal protection of the laws.

Sections 422.33 and 422.35 of the Code of Iowa are set out in the Appendix at A-1 to A-5.

QUESTION PRESENTED.

Does the Iowa income tax, with its apportionment formula based on ratio of Iowa sales to total sales, fall afoul the Commerce Clause or the Fourteenth Amendment's Due Process or Equal Protection Clauses, in the absence of any evidence that the formula effected a "grossly distorted result" as applied to the Appellant?

STATEMENT.

In view of the full statement of facts in the brief for the Appellee, we limit our statement to three matters of critical importance to the Court's disposition of this case.

First, it is patently false to suggest that the State of Iowa is seeking to tax the Moorman Manufacturing Company ("Moorman") on "100% of its income." Notwithstanding statements to this effect in appellant's brief, the fact is that in none of the tax years at issue did Iowa seek to impose a tax on more than 21.9% of Moorman's apportionable income. (Exh. 1-A, App. 34.) Furthermore, if one looks at the overall tax burden imposed by the State of Iowa upon Moorman in light of its total income, the percentages are even smaller. In none of the tax years at issue did Iowa seek to tax Moorman on more than 17% of its federal taxable income. (Exh. 1-A, App. 4.)[1]

Second, the focus of the controversy before this Court is Moorman's apportionable income, *i.e.*, that portion of Moorman's federal taxable income which must be apportioned in part to Iowa pursuant to an appropriate formula because its precise geographical source cannot be satisfactorily identified. Indeed, the most salient fact in this case may well be the complete absence in the record of any evidence indicating precisely where Moorman's income was actually earned. It is because one cannot on this record identify the sources of Moorman's earnings

1. The percentages were calculated by adding Moorman's assignable income to Moorman's income apportionable to Iowa and dividing by Moorman's Federal taxable income. In fact, the percentage figures in the text overstate the extent of Moorman's Iowa tax liability since only a small portion of Moorman's assignable income—dividends, interest, and the like—were actually assignable to Iowa. *See* Moorman's Income Tax Returns for 1968-1972. These returns are in the Record but were not included as part of the Appendix, and the calculations were therefore made on the basis of figures readily available to the Court.

— the profits it may have gained through operations in one State, the losses it may have suffered through operations in another — that resort to an apportionment formula is necessary to provide a rough approximation of the source of those earnings. Choice of a particular formula is merely a means of establishing that source for tax purposes.

Third, the stipulated facts of this case raise the question whether the Commerce Clause may be relied upon at all as a basis for invalidating the Iowa tax as applied to Moorman. The activities on which the tax was based were solely intrastate activities. According to the stipulated facts, Moorman's products were manufactured in Illinois and shipped to Moorman's warehouses in Iowa. (App. 24.) Sales in Iowa were made by Iowa salesmen and warehousemen from Moorman's Iowa warehouses to Iowa consumers. (App. 24.) These are not interstate sales. There is no interstate commerce affected by imposition of this tax. The fact that Moorman is a foreign corporation does not translate the tax into a burden on interstate commerce. The fact that, before the goods came to rest in Iowa warehouses, they made the journey from Illinois, does not make the Iowa sales into sales in interstate commerce. Hence, so far as Moorman is concerned, the tax in question here may be regarded as a tax on intrastate commerce only, with the measure of the tax a proportionate share of its net income.

SUMMARY OF ARGUMENT.

In the long history of constitutional litigation over the validity of formulas designed to apportion a just share of a multistate business's property or income to a taxing State, this Court has never held an apportionment formula unconstitutional on its face. And in those few instances in which the Court, after searching inquiry, has held the application of an apportionment formula to a particular taxpayer unconstitutional, it has done so only on the basis of an overwhelming evidentiary showing by the taxpayer that the formula in question actually produced a grossly distorted result. The Court's traditional reluctance to tamper with State apportionment formulas is not an historical accident. Rather it stems from fundamental principles to which the Court has consistently adhered. These principles lie at the heart of our federal system as they involve a proper respect for State taxing power as well as an appreciation of the appropriate role of the judiciary in keeping that power within constitutional bounds. Unless this Court is to ignore these principles and in effect abandon a century of precedent, the exercise of Iowa's tax power in this case must be sustained.

In evaluating the contention under the Due Process Clause that an apportionment formula attributes more property or income to a taxing State than it may rightly claim, this Court has invariably emphasized two points. First, the Court has recognized that the very nature of the undertaking—the resort to a mathematical formula to determine the State's share of a business entity's tax base where there is no satisfactory way of determining it directly—involves rough approximation. The Court has repeatedly held that the Due Process Clause requires nothing more exacting. Second, and following naturally from the first point, the Court has made it plain that a taxpayer challenging an apportionment formula has more than the usual heavy burden

of proving by clear and convincing evidence that the application to it of the formula produces a grossly disproportionate result. This is never accomplished by hypothetical examples or merely showing the possibility of unfairness. Rather it can be demonstrated only by a powerful evidentiary showing that as applied to a particular taxpayer the operation of the formula is palpably unfair. A faithful implementation of these principles requires, as the Supreme Court of Iowa held, that the State's apportionment formula be sustained as constitutional on its face. These principles likewise support the determination, which the Supreme Court of Iowa made,[2] that the record in this case wholly fails to establish the gross deviation from a reasonable apportionment that is necessary to invalidate an apportionment formula as applied to a particular taxpayer.

Even if it is assumed that interstate commerce is involved in this case,[3] the criteria for evaluating the constitutionality of the apportionment formula under the Commerce Clause do not differ in substance from those under the Due Process Clause, as this Court has stated on a number of occasions. And for essentially the same reasons, settled constitutional doctrine requires, as the Supreme Court of Iowa held, that the Iowa apportionment formula be sustained on its face and as applied under the Commerce Clause. Indeed, this Court has upheld, over both Commerce Clause and Due Process Clause objections, much more sweeping exercises of State tax power than are even alleged in this case. For the Court to hold the exercise of such power unconstitutional in this case would amount to

2. 254 N. W. 2d at 753-54 (A-137-A-139). In light of the great reliance placed by Appellant on the so-called "findings" of the Iowa district court, it should be noted that review in the Iowa Supreme Court in equity actions, such as the instant case, is *de novo*. Iowa Const., Art. V, § 4; Iowa Code, § 422.29, § 686.2; Rule of Civil Procedure 334, repealed 1 July 1977, after the close of this litigation, and replaced by Rule of Appellate Procedure 4. Thus, it is the findings of the Iowa Supreme Court, not those of the inferior tribunal, that are controlling for purposes of this appeal.

3. The sales on which the tax is based were all made from goods in Appellant's warehouse to Iowa purchasers. See p. 5, *supra*.

the effective overruling of a large number of its precedents—some of them of recent vintage—and would constitute a wholesale and unwarranted uprooting of the framework which for years has been the basis of adjudication of the constitutional limitations on the exercise of State tax power.

The challenge to the Iowa apportionment formula on Equal Protection grounds is plainly insubstantial. The States are accorded the utmost leeway in making classifications for tax purposes, as recent decisions of this Court demonstrate. Hence, even accepting Moorman's suggestions that the legislature has made the classifications of which it complains, they are unobjectionable from a constitutional standpoint.

Moorman's case rests primarily on dicta drawn from this Court's opinion in *General Motors Corp.* v. *District of Columbia*, 380 U. S. 553 (1965), which invalidated the District of Columbia's single-factor apportionment formula. But that decision provides only superficial support for Moorman's position here, since the Court explicitly refrained from reaching the constitutional issues sought to be raised in that case. The decision, therefore, cannot be invoked to justify a holding that an apportionment formula is unconstitutional on its face in the teeth of controlling constitutional precedent to the contrary. Nor does it provide any support for a finding that the statute is unconstitutional in its application to the taxpayer here in light of the insufficiency of this record to sustain such a finding.

As this Court has many times acknowledged, it has neither the constitutional power nor institutional capability to play anything but a limited role in reviewing the propriety of formulas designed to apportion a share of a multi-state enterprise's tax base to the taxing State. Other than taking the extraordinary step of invalidating the application of a formula in that rare case when a taxpayer has been able to demonstrate by clear and cogent evidence that the formula has a produced a grossly distorted result—evidence of which this record is totally barren—the Court has accordingly refrained from interfering with the

application of State apportionment formulas. It has done so in the recognition that—absent congressional legislation imposing a uniform formula—variations in such formulas are to be expected and, from a constitutional standpoint, must be tolerated. For this Court to hold that the Iowa apportionment formula is unconstitutional because it varies in some respects from formulas currently in vogue in other States would be in effect to impose upon all States the requirement of adopting a particular formula to apportion corporate income. Such a step would be wholly inconsistent with this Court's constitutional tradition and would arrogate to itself the power to act affirmatively under the Commerce Clause—a power that is confided solely to Congress by the Constitution. In light of Congress' failure to act in this area, despite repeated consideration as to whether it should do so, it would be especially unseemly for this Court to take the unprecedented step of effectively imposing a uniform apportionment formula upon the States, even if such action were within the scope of its constitutional power.

ARGUMENT.

I.

THE STATUTORY REQUIREMENT THAT NET INCOME BE APPORTIONED TO IOWA BY THE RATIO OF IOWA SALES TO TOTAL SALES IS CONSTITUTIONAL ON ITS FACE UNDER THE DUE PROCESS CLAUSE AND THE COMMERCE CLAUSE.

Moorman has challenged the constitutionality of the apportionment provision of the Iowa corporate income tax under both the Due Process Clause and the Commerce Clause. It must be recognized that there is considerable overlap in the constitutional analyses under these Clauses. Indeed, as this Court recently remarked in the context of a constitutional challenge to a State apportionment formula on both Due Process and Commerce Clause grounds:

> "The problem under the Commerce Clause is to determine 'what portion of an interstate organism may appropriately be attributed to each of the various states in which it functions.' *Nashville, C. & St. L. R. Co.* v. *Browning*, 310 U. S. 362, 365. So far as due process is concerned the only question is whether the tax in practical operation has relation to opportunities, benefits, or protection conferred or afforded by the taxing State. See *Wisconsin* v. *J. C. Penney Co.*, 311 U. S. 435, 444. Those requirements are satisfied if the tax is fairly apportioned to the commerce carried on within the State." *Ott* v. *Mississippi Valley Barge Line Co.*, 336 U. S. 169, 174 (1949). Neither appellants nor appellees contend that these two analyses bear different implications insofar as our present case is concerned. [*Norfolk & Western Ry.* v. *State Tax Commission*, 390 U. S. 317, 325 n. 5 (1968).]

Although the Due Process Clause and Commerce Clause challenges to the constitutionality of the statute are addressed separately here, much of what will be said under the rubric of Due Process is equally applicable to the Commerce Clause. To avoid repetition, discussion of the Commerce Clause will be limited to any additional constitutional limitations arguably imposed by that Clause on the State's power to apportion net income.

A. The Iowa Formula for Apportioning Net Income to the State Is Constitutional on Its Face under the Due Process Clause.

The Due Process Clause standards for evaluating an apportionment formula are largely shaped by the underlying reason for using such a formula in the first place. Where an enterprise carries on a single integrated business both within and without the State, its tax base generally cannot satisfactorily be identified or segregated on a geographical basis. See ALTMAN & KEESLING, ALLOCATION OF INCOME IN STATE TAXATION 107 (2 ed. 1950). Due to the impracticability of so identifying or segregating the tax base of such an enterprise—referred to as a "unitary business"—resort is made to apportionment formulas as a rough means of attributing a reasonable share of the tax base to the taxing State. These considerations are especially pertinent to the taxation of net income, which is at issue here. For, as the Court has observed, the net income or profits of a business frequently are "earned by a series of transactions beginning with manufacture in [one state] and ending with sale in other States" and "[t]he legislature, in attempting to put upon this business its fair share of the burden of taxation [is] faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders." *Underwood Typewriter Co.* v. *Chamberlain*, 254 U. S. 113, 120-21 (1920).[1]

1. The Iowa apportionment provisions faithfully reflect these principles. The statute defines a "Unitary business" as a "business carried on partly within and partly without a state where the portion of the business carried on within the state depends on or contributes to the business outside the state." Iowa Code § 422.32(6). Only a

(Footnote continued on next page.)

It is in view of the underlying rationale for applying an apportionment formula to a multistate enterprise's overall tax base that the governing constitutional principles become clear and comprehensible. Ever since this Court approved the use of a rail mileage formula as a "just and equitable method" of ascertaining the proportion of a corporation's property taxable by a State, *Pullman's Palace Car Co.* v. *Pennsylvania,* 141 U. S. 18, 26 (1891), it has recognized that such formulas, which owe their very existence to the absence of exact alternatives for dividing the tax base of a unitary business, cannot be expected to achieve precision.

> [T]his Court has long realized the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities . . . and has declared that "rough approximation rather than precision is sufficient." *Illinois Central Ry.* v. *Minnesota,* 309 U. S. 157, 161. [*International Harvester Co.* v. *Evatt,* 329 U. S. 416, 422 (1947).]

Time and again this Court has emphasized that "by its very nature the problem is incapable of precise and arithmetical solution," and that "exactness is concededly unobtainable." *Nashville, C. & St. L. R. Co.* v. *Browning,* 310 U. S. 362, 365-66 (1940). As a logical corollary, the Court has therefore refused to upset the application of State apportionment formulas without a showing by the taxpayer that the apportionment is in fact "out of all appropriate proportion to the business transacted," *Hans Rees' Sons, Inc.* v. *North Carolina* ex rel. *Maxwell,* 283 U. S. 123, 135 (1931), or produces a "grossly distorted result." *Norfolk & Western Ry.* v. *State Tax Comm'n,* 390 U. S. 317, 326 (1968).

In light of the constitutional criteria for evaluating apportionment formulas, it is apparent why the Court has never held

(Footnote continued from preceding page.)
corporation carrying on such a unitary business in Iowa is required to determine its net income attributable to the State by an apportionment formula, and the regulations refer to Supreme Court authority for guidance in determining whether a business is unitary. See Iowa Admin. Code § 730-54.8 (422), referring to *Butler Bros.* v. *McColgan,* 315 U. S. 501 (1942).

such a formula unconstitutional on its face and why there is no basis for doing so in this case. To hold that an apportionment formula is unconstitutional "on its face," as Moorman urges the Court to do here (Appellant's Br. 21), is to make the judgment that such a formula by its very terms will necessarily produce a "grossly distorted result" or an apportionment "out of all proportion to the business transacted." But how can one make the judgment that a formula will necessarily produce an apportionment "out of all proportion to the business transacted" without actually examining the business transacted and comparing it with the result produced? The answer is that as a matter of constitutional law one cannot make such a judgment—at least with respect to the type of apportionment formulas this Court has heretofore considered and sustained which includes the very formula at issue here.[2] For if there is any single principle that emerges from this Court's numerous decisions regarding State apportionment formulas, it is that due regard for State taxing power and recognition of the imprecision inherent in any attempt to apportion a unitary enterprise's tax base requires that the constitutionality of such formulas be evaluated as applied to the particular taxpayer.

Examination of the Court's decisions upholding apportionment formulas based on such factors as track mileage,[3] barge line mileage,[4] designated assets,[5] gross receipts,[6] property,[7] and payroll,[8] — all of which are by definition constitutional on their

2. See *Ford Motor Co.* v. *Beauchamp,* 308 U. S. 331 (1939).

3. See, *e.g., Pullman's Palace Car Co.* v. *Pennsylvania,* 141 U. S. 18 (1891).

4. See, *e.g., Ott* v. *Mississippi Barge Line Co.,* 336 U. S. 169 (1949).

5. See, *e.g., Bass, Ratcliff & Gretton* v. *State Tax Commission,* 266 U. S. 271 (1924).

6. See, *e.g., Ford Motor Co.* v. *Beauchamp,* 308 U. S. 331 (1939).

7. See, *e.g., Underwood Typewriter Co.* v. *Chamberlain,* 254 U. S. 113 (1920).

8. See, *e.g., Butler Bros.* v. *McColgan,* 315 U. S. 501 (1942).

face — reveals the consistency with which the Court has adhered to this principle. It is demonstrated even more strikingly in those rare instances in which the Court has found that the application of the particular formula exceeded constitutional bounds. Thus in the single case in the last forty years in which the Court has found the application of an apportionment formula unconstitutional, *Norfolk & Western Ry.* v. *State Tax Commission,* 390 U. S. 317 (1968), the Court could not have been more explicit in the limited nature of its holding. Noting that it was dealing with the "familiar mileage formula" whose application it has sustained in "various contexts," 390 U. S. at 320, 326[9] and that the taxpayer must bear the usual "heavy burden" in challenging the application of such a formula, *id.* at 326, the Court found that the taxpayers had carried the burden by demonstrating that the "application of the mileage formula led to a grossly distorted result," and that the State "made no effort to offset the convincing case that they have made." *Ibid.* At the same time, the Court reiterated that its "decisions recognize the practical difficulties involved and do not require any close correspondence between the result of computations using the mileage formula and the value of property actually located in the State. . ." *Id.* at 327. The Court's holding thus reaffirmed the essential point that the constitutionality of apportionment formulas cannot properly be evaluated "on their face" but must be considered in the context of their application to the particular taxpayer who is charged with the heavy evidentiary burden of demonstrating that the formula has led to a "grossly distorted result."

The impropriety of evaluating the constitutionality of an apportionment formula by reference to its terms alone is particularly egregious in connection with the apportionment of net income, as in the instant case. In dealing with the overall net income of a unitary business, a State is faced not merely with the practical problems of directly segregating the tax base on a geographical basis, as was the case in *Norfolk & Western* v. *State Tax Comm'n* with respect to the railroad's rolling stock, but often with the virtual "impossibility of allocating specifically the profits earned by the processes within its borders." *Underwood Typewriter Co.* v. *Chamberlain,* 254 U. S. 113, 121 (1920). When the net income to be apportioned is in essence the net income reported on a multistate business's federal tax return, as it is in this case (Exh. 1-A, App. 34), there is ordinarily no way of determining, at least on an *a priori basis,* in which State such net income is earned. Perhaps all of the net gain of an integrated enterprise like Moorman, which engaged in both the manufacture and sale of its products, is in fact derived exclusively from the exploitation of particularly favorable markets in certain States. Indeed, it might well be the case that if selling profit could be considered separately, the enterprise's net income would be higher than it would be when such activity is considered in conjunction with less efficient manufacturing activities that might have been operating at a loss. To be sure, it is precisely because one cannot examine these activities separately to ascertain the exact source of the profits that one employs an apportionment formula to begin with. But given the premise, to hold that a formula for apportioning net income is "facially unconstitutional" is to make a judgment that wherever the true sources of an enterprise's net income may lie, an attempt to establish them by the formula in question will necessarily produce a "grossly distorted result."

Such a conclusion is plainly untenable here. In the example suggested above, in which all the profits of an enterprise are attributable to the existence of the favorable market where the sales are made, it could hardly be contended that the apportionment of such net income on the basis of sales produces a "grossly distorted result." And, if that is true the statute cannot be un-

9. The statute in question, quoted at 390 U. S. 320-21 provided ". . . when any railroad shall extend beyond the limits of this state and into another state in which a tax is levied and paid on the rolling stock of such road, then the said commission shall assess, equalize and adjust only such proportion of the total value of all rolling stock of such railroad company as the number of miles of such road in this state bears to the total length of the road as owned or controlled by such company."

constitutional on its face because it will not necessarily produce such a result. Moreover, since the very premise underlying the use of a formula to apportion net income is that one does not in fact know where such income is actually earned, one simply cannot say on an *a priori* basis that in any case the result produced will not constitute a "rough approximation" of the actual source of the enterprise's earnings, which, as indicated above, is all the Constitution demands. This does not preclude a taxpayer from attempting to demonstrate by clear and cogent evidence that the apportionment formula as applied has in fact produced a "grossly distorted result" and is therefore unconstitutional. See pp. 22-37, *infra*. But to hold that an apportionment formula is unconstitutional as applied after such a showing has been made is very different from holding such a formula unconstitutional on its face, as is urged here.

Any conceivable doubt about the constitutionality of Iowa's apportionment formula on its face is laid to rest by controlling precedent. First, not a single decision of this Court can be cited for the proposition that a net income apportionment formula —or indeed any apportionment formula—is unconstitutional on its face, for the simple reason that this Court has never so held. The absence of any such holding is no historical accident. Rather, it stems from fundamental considerations relating to the proper respect for State taxing power and the conceded impossibility of achieving precise results. See, *e.g.*, *Nashville, C. & St. L. R. Co.* v. *Browning*, 310 U. S. 362, 365-66 (1940).

Second, in those cases where the Court has considered the application of apportionment formulas to the net income of particular taxpayers, it has made it clear that the Constitution does not limit the States with respect to the type of formula they may employ to apportion net income. Thus, the Court has upheld formulas for apportioning net income based on the ratio of a taxpayer's in-state property to its property wherever located, *Underwood Typewriter Co.* v. *Chamberlain*, 254 U. S. 113 (1920); *Kent-Coffey Mfg. Co.* v. *Maxwell*, 291 U. S. 642

(1934), *aff'g per curiam* 204 N. C. 365, 168 S. E. 397 (1933); and of a taxpayer's designated in-state assets to such assets wherever located, *Bass, Ratcliff & Gretton* v. *State Tax Commission*, 266 U. S. 271 (1931); and of a taxpayer's in-state property, payroll, and sales to such property, payroll, and sales wherever located. *Butler Bros.* v. *McColgan*, 315 U. S. 501 (1942). Inasmuch as these formulas for apportioning net income have thus been held constitutional on their face (as well as in application), one can hardly conclude that the Constitution requires the States to apportion net income pursuant to any particular formula or to include a specified type or number of factors in the formula. Indeed, on the one occasion that the Court did find that the application of an apportionment formula to a taxpayer's net income[10] produced a result "out of all appropriate proportion to the business transacted" by the taxpayer in the state, *Hans Rees' Sons* v. *North Carolina* ex rel. *Maxwell*, 283 U. S. 123, 135 (1931), the apportionment was made under the very formula which the Court had upheld previously, see *Underwood Typewriter Co.* v. *Chamberlain, supra*, and would uphold again, see *Kent-Coffey Mfg. Co.* v. *Maxwell, supra*. Thus it is plainly in their application—and never by their terms alone —that the constitutionality of apportionment formulas must be evaluated.

Finally, one cannot ignore the Supreme Court's decision in *Ford Motor Co.* v. *Beauchamp*, 308 U. S. 331 (1939). The Court there sustained on its face and as applied the very apportionment formula at issue here, one based on the ratio of gross receipts from business done in the state to gross receipts from the entire business. While the formula was employed to apportion the taxpayer's capital stock, surplus, undivided profits, and long-term obligations,[11] rather than its net income, there is

10. *Norfolk & Western* v. *State Tax Comm'n* was not concerned with a net income tax.

11. The tax at issue was "based upon that proportion of the outstanding capital stock, surplus and undivided profits, plus the

(Footnote continued on next page.)

nothing in the case to suggest that the Court's holding—sustaining the constitutionality of an apportionment formula based on gross receipts—would be inapplicable to a tax upon net income. Notwithstanding Moorman's suggestion that the case is "irrelevant" because it does not deal with a net income tax (Appellant's Br. 24), the Court's opinion suggests quite the opposite. It explicitly relies on cases involving the taxation of net income in upholding the levy at issue, see 308 U. S. at 335 (citing *Underwood Typewriter Co.* v. *Chamberlain, supra,* and *Bass, Ratcliff & Gretton* v. *State Tax Commission, supra*). Moreover, its language suggests that to restrict the decision's import to the particular type of tax or formula there involved would be to take an impermissibly crabbed approach to the scope of State tax power. Hence it rejected the taxpayer's contention that "the constitutionality of state taxation turns on so narrow an issue as whether local assets rather than local gross receipts are used in a taxing formula." *Id.* at 336.

B. The Iowa Formula for Apportioning Net Income to the State Is Constitutional on Its Face under the Commerce Clause.

As indicated above (see pp. 10-11, *supra*), many of the considerations that were discussed under the rubric of Due Process are equally applicable to an evaluation of the constitutionality of an apportionment formula under the Commerce Clause. Indeed, in many of the cases cited in the preceding discussion, the taxpayer attacked the constitutionality of the formula on both Due Process and Commerce Clause grounds and the Court dealt with both contentions, often without distinguishing between the two. See *Underwood Typewriter Co.* v. *Chamberlain,* 254 U. S. 113 (1920); *Bass, Ratcliff & Gretton* v.

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amount of outstanding bonds, notes and debentures, other than those maturing in less than a year from date of issue, as the gross receipts from its business done in Texas bears to the total gross receipts of the corporation from its entire business." 308 U. S. at 332-33.

State Tax Commission, 266 U. S. 271 (1924); *Ford Motor Co.* v. *Beauchamp,* 308 U. S. 331 (1939); *Nashville C. & St. L. R. Co.* v. *Browning,* 310 U. S. 362 (1940); *International Harvester Co.* v. *Evatt,* 329 U. S. 416 (1947); *Ott* v. *Mississippi Barge Line Co.,* 336 U. S. 169 (1949); *Norfolk & Western Ry.* v. *State Tax Commission,* 390 U. S. 317 (1968). Although the verbal formulation of the issue under the two Clauses may differ, the substantive inquiry is essentially the same. If the application of an apportionment formula results in the taxation of property or income with which the State has no connection in violation of the Due Process Clause, it will likely impose a burden upon or result in the multiple taxation of interstate commerce in violation of the Commerce Clause.[12] And if the taxing power of the State is exercised through the use of an apportionment formula within the broad limits defined by the Due Process Clause, it is unlikely to offend the requirements of the Commerce Clause.

The traditional invulnerability of State apportionment formulas to attacks on their "facial" constitutionality embraces both Commerce and Due Process Clause challenges, as the cases cited in the preceding paragraph demonstrate. To conclude that the Iowa apportionment formula violates the Commerce Clause on its face, one would have to determine that the net income apportioned to Iowa under the formula will necessarily produce a "grossly distorted result," thus burdening interstate commerce or subjecting it to multiple taxation. But, as explained above (see pp. 11-13, *supra*), the very reason one apportions the net income of a unitary business like Moorman's is that no one knows precisely where it was earned. To conclude that the sales-factor formula is unconstitutional on its face is to conclude that the profits apportioned to the taxing State by the formula could not in fact have been earned there. Such a conclusion is plainly

12. As the Court put it in *Norfolk & Western Ry.* v. *State Tax Commission,* 390 U. S. at 325: "The taxation of property not located in the taxing State is constitutionally invalid, both because it imposes an illegitimate restraint on interstate commerce and because it denies to the taxpayer the process that is his due."

untenable, for reasons already explained which need not be repeated here. (See pp. 14-16, *supra.*) It is sufficient for present purposes to note that "rough approximation rather than precision," is the constitutional criterion for judging the validity of apportionment formulas under the Commerce Clause as well as the Due Process Clause, see *Illinois Central R. R.* v. *Minnesota,* 309 U. S. 157, 161 (1940); *Nashville, C. & St. L. R. Co.* v. *Browning,* 310 U. S. 362, 365-66 (1940), and there is no basis for invalidating the Iowa apportionment formula as unconstitutional on its face under the Commerce Clause.

C. The Court's Opinion in General Motors Corp. v. District of Columbia, 380 U. S. 553 (1965), Does Not Control Resolution of the Constitutional Issues Raised by this Appeal.

The foregoing analysis is essentially unaffected by *General Motors Corp.* v. *District of Columbia,* 380 U. S. 553 (1965), on which Moorman principally relies. *General Motors* involved the District of Columbia franchise tax, which was measured by net income. In contrast to the provision of the Iowa statute here at issue which reflects a deliberate legislative judgment as to the appropriate method of apportionment, the District of Columbia tax statute left the question of apportionment methods to the discretion of the tax commissioners. That discretion, however, was limited by the statutory directives that "[t]he measure of the franchise tax shall be that portion of the net income of the corporation . . . as is fairly attributable to any trade or business carried on or engaged in within the District . . . ," and that "[i]f the trade or business of any corporation . . . is carried on or engaged in both within and without the District, the net income derived therefrom shall . . . be deemed to be income from sources within and and without the District." 380 U. S. at 554-55. The commissioners promulgated regulations that apportioned the income of certain corporations, which included General Motors, to the District by the percentage that "District

sales made during the taxable year bear to the total sales made everywhere during such taxable year." *Id.* at 555.

General Motors made substantial sales in the District but carried on no manufacturing operations there. It challenged the commissioners' apportionment regulations on the grounds that the apportionment of its income to the District solely on the basis of a sales factor was inconsistent with the statute as well as the Due Process and Commerce Clauses. Refusing to address the constitutional issues, this Court held that the regulations providing for apportionment by a single-factor sales formula were not authorized by the statute. The Court read the statute to require not only that the income of a corporation doing business within and without the District be apportioned, as the United States Court of Appeals had held, but to require in addition the apportionment of that particular portion of a corporation's income earned from manufacture outside and sales inside the District.

For a number of reasons, the *General Motors* decision is of limited significance here. First and foremost, the Court's decision was not based on constitutional grounds. The Court could not have been more explicit on this point, noting that it did not take "any position on the constitutionality of a state income tax based on the sales factor alone," and that it had "refrained from attempting to define any single appropriate method of apportionment." 380 U. S. at 561. Thus, the case simply does not stand for the proposition that the apportionment formula there at issue —let alone the formula at issue in this case— is unconstitutional on its face. Secondly, the statutory language on which decision turned in *General Motors* was not the provision making "net income . . . as is fairly attributable" to the District taxable; rather it was the specific requirement that net income derived from a trade or business carried on within and without the District shall "be deemed to be income from sources within and without the District." It was the Court's interpretation of this statutory phrase—which has no analogue in the Iowa statute

and can scarcely be found in the Due Process or Commerce Clauses—which was the fulcrum of the Court decision. Third, while the Court in dicta expressed some concern that the Districts' formula was not consistent with those generally prevailing in other jurisdictions, these general observations made in support of its reading of the District of Columbia statute simply cannot be translated into constitutional imperatives in light of the specific disavowal by the Court of any intention of reaching the constitutional questions potentially raised. Finally, even reading *General Motors* as a constitutional opinion would not lend support to Moorman's contention here that the Iowa statute is unconstitutional on its face. In light of the evidentiary showing made by General Motors and the findings of the trial court there, the decision would stand for no more than the established principle that when an apportionment formula produces a "grossly distorted result," it may be struck down as unconstitutional in its application to a particular taxpayer.

II.

THE STATUTORY REQUIREMENT THAT NET INCOME BE APPORTIONED TO IOWA BY THE RATIO OF IOWA SALES TO TOTAL SALES IS CONSTITUTIONAL AS APPLIED TO MOORMAN UNDER THE DUE PROCESS CLAUSE AND THE COMMERCE CLAUSE.

In addition to alleging that the Iowa apportionment formula is unconstitutional on its face, Moorman contends that the formula is unconstitutional in its application to Moorman. The Iowa Supreme Court, which reviewed the evidence *de novo*,[1] found that Moorman had failed to carry its evidentiary burden of establishing that the formula in its application to Moorman was either unreasonable or arbitrary.[2] The Iowa Supreme Court's

1. See page 7, note 2, *supra*.

2. 254 N. W. 2d at 753-54 (App. 137-39). In this connection two points should be kept in mind. First, the trial court never reached the issue of the constitutionality of the Iowa apportionment

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determination was required by the governing constitutional precedents and should be sustained by this Court.

A. The Iowa Formula for Apportioning Net Income to the State Is Constitutional as Applied to Moorman under the Due Process Clause.

The fundamental issue in any constitutional challenge to the application of a State apportionment formula is whether the taxpayer has met the extraordinary burden of showing by "clear and cogent evidence" that the apportionment produces a "grossly distorted result" or one "out of all appropriate proportion to the business' transacted by the taxpayer in the State. See *Norfolk & Western Ry.* v. *North Carolina* ex rel. *Maxwell*, 297 U. S. 682, 688 (1936); *Norfolk & Western Ry.* v. *State Tax Commission*, 390 U. S. 317, 329 (1968); *Hans Rees Sons, Inc.* v. *North Carolina* ex rel. *Maxwell*, 283 U. S. 123, 135 (1931). Time and again this Court has reiterated that the constitutional standards are not unduly exacting, see, *e.g.*, *Butler Bros.* v. *McColgan*, 315 U. S. 501, 506 (1942), as indeed they cannot be in an area where "exactness is concededly unobtainable." *Nashville, C. & St. L. R. Co.* v. *Browning*, 310 U. S. 362, 365-66 (1940). These controlling principles, which have been given concrete expression on numerous occasions, fully support the Iowa Supreme Court's determination that Moorman has failed to carry its heavy burden to prove that the application to Moorman of the State's apportionment formula is unconstitutional.

Moorman is a nationwide enterprise engaged in the manufacture and sale of livestock and poultry feed products. Its sales

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formula in its application to Moorman, because it had resolved the issues before it in terms of the facial constitutionality of the statute. (App. 56-98.) Thus we have no factual findings of the Iowa trial court with respect to this issue. Second, it is clear, in any event, that no reliance may be placed on the findings of the district court—in whatever context made—since in equity cases the Iowa Supreme Court exercises *de novo* review and thus its findings, rather than those of the trial court, are controlling on this appeal. See page 7, note 2, *supra*.

activities span more than thirty States, including Iowa, where it makes substantial sales. The products sold in Iowa are manufactured in Illinois. Moorman's argument that the Iowa apportionment formula is unconstitutional as applied rests essentially on the allegation that the Iowa formula compels a foreign producer like Moorman to "pay tax on 100% of [its] income from Iowa business already heavily, and properly, taxed in other states." (Appellant's Br. 20.) To support this assertion, Moorman relies ultimately on the findings of the Iowa district court that, as Moorman puts it, "[t]he Iowa single-factor formula taxed 100% of the income from each dollar of sales of Moorman's goods into Iowa, although 75% of payroll and 30% of capital are used in the manufacture of goods (in Illinois) . . . and resulted in 'gross overreaching' by the State." *Id.* at 5. As indicated above, the relevance of the Iowa district court's findings for purposes of this appeal is highly questionable. See page 7, note 2, *supra*. Nevertheless, assuming *arguendo* that such findings (and Moorman's contentions based on them) may be considered by this Court, it is plain that they cannot withstand analysis.

Under the Iowa corporate income tax statute, it is indisputable that the only "income" of a taxpayer like Moorman that is ever subject to apportionment is a specified portion of such taxpayer's federal taxable income.[3] Thus, the single-factor sales formula, which is employed to apportion a fair share of Moorman's income to Iowa, is applied neither to Moorman's gross income, nor to the income that Moorman may have earned in its operations in Illinois and Iowa. Rather, it is applied directly to a portion of Moorman's overall federal taxable income and thus represents an attempt to apportion to Iowa a share of Moorman's overall net income or profits attributable to Iowa operations.

In light of the way the Iowa apportionment scheme actually operates, the fundamental misconception underlying appellant's

3. See Iowa Code §§ 422.33, 422.35 (reproduced in Appellant's Br., App. B, A1-A5); Exh. 1-A (App. 34).

reasoning becomes apparent. As noted above, Moorman relies on the trial court's finding that "because the Iowa single sales factor tax admits of neither property nor payroll inputs in Illinois plant and labor as part of its formula, each dollar of sales of Moorman's goods in Iowa is taxed at 100% while nearly 75% of Moorman's payroll and 30% of its capital is used in the manufacture of goods taxed here." App. 76; Appellant's Br. 5. This assumes that the net income actually taxed by Iowa can be directly correlated with the sales, property, or payroll that may be factors in the formula designed to apportion such income. But such an assumption flies in the face of the facts. Each "dollar in sales of Moorman's goods in Iowa" is not taxed at all—contrary to Moorman's statement. Rather, each dollar in sales is used simply to apportion a small fraction of Moorman's net income to Iowa.[4] Whether in fact that particular sales dollar produced more or less net income from Moorman in Iowa than is apportioned pursuant to the formula is something that we simply do not know—at least not on this record. For there is nothing in the record which shows the precise source of any of Moorman's net income. Rather, as in *Underwood Typewriter Co.* v. *Chamberlain*, 254 U. S. 113 (1920), the "profits of the corporation were largely earned by a series of transactions beginning with manufacture in [one State] and ending with sale in other States" with the consequent "impossibility of allocating specifically the profits earned by the processes conducted" within one State's borders. *Id.* at 120-21.

Nevertheless, Moorman argues that the Iowa formula "fails to allow a reasonable apportionment of income associated with Iowa sales to be attributed to Illinois. . . ." (Appellant's Br. 30.) But in light of the impossibility—at least on this record—of identifying the precise sources of that portion of Moorman's overall federal net income to which the Iowa apportionment formula is actually applied, one cannot reasonably conclude that the single-factor sales formula fails fairly to apportion

4. Moorman's gross sales for the years in question averaged over $100,000,000. See Exh. 1-C (App. 36).

Moorman's net income. Merely because capital and labor outside Iowa have produced the product sold inside Iowa does not imply that any of the net income or profits from the ultimate sale are attributable to the manufacturing activities. For all that appears in the record, it could well be the case that it was only as a result of a highly favorable Iowa market that any net income was obtained at all from sales of Illinois-produced products. Thus, the attribution of Moorman's net income to Iowa on the basis of its sales-factor formula could actually underrepresent the profit attributable to Iowa, since it would not take into account the Illinois losses that had been offset by the Iowa gains before any net profits were even realized. This is not to argue that such was in fact the case. The point is simply this: the record does not reveal the precise sources of Moorman's overall net income, which could be attributable in whole or in part to its operations in any of over thirty states; that the Iowa apportionment formula was applied only to such overall net income, not gross sales; and that it is therefore impossible to say with any degree of confidence—and certainly not with that degree of confidence necessary to sustain a Due Process objection—that the net income apportioned pursuant to the Iowa formula was not fairly attributable to activities carried on by Moorman in Iowa.

This conclusion is reinforced by an examination of the decisions of this Court that have considered this problem. The Court has decided six cases involving challenges to the apportionment of a multistate enterprise's net income. The first was *Underwood Typewriter Co.* v. *Chamberlain*, 254 U. S. 113 (1920). Underwood, like Moorman, manufactured and sold tangible personal property, with its activities spread out over a number of states. The State of Connecticut in that instance, like the State of Iowa here, sought to tax Underwood on a share of its net income attributable to its Connecticut operations. The net income in that case, like the net income here, was ascertained by reference to the corporation's federal taxable income. The Connecticut

formula which was applied to such net income to apportion a share to the State, like the Iowa formula here at issue, was based on a single ratio. The ratio employed was real and tangible personal property in the State to such property wherever located, which produced a Connecticut percentage of 47 percent. Underwood challenged the application of the apportionment formula to it on both Due Process and Commerce Clause grounds, arguing that since only about 3 percent of its profits were received from sales and other activities in Connecticut, it was improper to base the tax upon 47 percent of its entire net income. The Court rejected the contention in the language cited frequently in this brief:

> [Underwood's] showing wholly fails to sustain the objection. The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut and ending with sale in other States. In this it was typical of a large part of the manufacturing business conducted in the State. The legislature in attempting to put upon this business its fair share of the burden of taxation was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It, therefore, adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the State. [254 U. S. 120-21.]

Four years after the *Underwood* decision, the Court again had occasion to consider a constitutional challenge to the apportionment of a tax based on net income in *Bass, Ratcliff & Gretton* v. *State Tax Commission*, 266 U. S. 271 (1924). The taxpayer was engaged in the brewing and sale of Bass' ale. All of the brewing was done in England, but it sold some of its products in New York, which sought to impose a tax upon a portion of the taxpayer's net income. As in *Underwood* and the instant case, the formula employed to apportion income to New York was based on a single factor, in this case the proportion of designated assets in New York to designated assets wherever located. As in *Underwood* and the instant case, the taxpayer

challenged the application of the formula to it on both Due Process Clause and Commerce Clause grounds, claiming, among other things, that because it had no federal net income—the net income to be apportioned was its world-wide income—New York must have been taxing income arising from business conducted outside the State. The Court, relying on its decision in *Underwood*, rejected the taxpayer's contentions in language that is relevant to the issue here:

> So in the present case we are of opinion that, as the Company carried on the unitary business of manufacturing and selling ale, in which its profits were earned by a series of transactions beginning with the manufacture in England and ending in sales in New York and other places—the process of manufacturing resulting in no profits until it ends in sales—the State was justified in attributing to New York a just proportion of the profits earned by the Company from such unitary business. . . .
>
> It is not shown in the present case, any more than in the *Underwood* case, that this application of the statutory method of apportionment has produced an unreasonable result. The fact that the Company may not have had any net income upon which it was subject to payment of income tax to the Federal Government, obviously does not show that it received no net income from the business which it carried on in New York. There is no evidence in the record as to whether the Company received any net income from its New York business, or the amount of the profit and loss on that business, if any, either considered separately or in connection with the manufacturing business carried on in Great Britain. [266 U. S. at 282-83.]

The analogy to the instant case could hardly be closer—in light of Moorman's contention that the Iowa apportionment formula "fails to allow a reasonable apportionment of income associated with Iowa sales to be attributed to Illinois. . . ." (Appellant's Br. 30.) As in *Bass*, there is no evidence in the record as to whether the Company received any net income from its Illinois business or the amount of profit or loss on that business, if any,

either considered separately or in connection with the sales operations carried on in Iowa.

The next opportunity the Court had to consider a net income tax apportionment was in *Hans Rees' Sons, Inc.* v. *North Carolina* ex rel. *Maxwell*, 283 U. S. 123 (1931). As in the previous cases, the State sought to tax a portion of the overall net income of a manufacturer and seller of tangible personal property on the basis of a single-factor formula, here the ratio of real and tangible property located in North Carolina to such property wherever located. Again, the taxpayer challenged the application of the formula to its net income under the Due Process and Commerce Clauses. But there was a striking difference from the previous cases in the nature of the taxpayer's attack. In place of the generalized allegations and speculative observations concerning the purported source of the taxpayer's net income, the taxpayer produced clear and cogent evidence of the specific source of its profits—evidence which demonstrated that the apportionment formula in question that attributed "to North Carolina a percentage out of all appropriate proportion to the business transacted" by the taxpayer in the State. 283 U. S. at 135. Thus, the taxpayer specifically demonstrated that its profit was derived from buying profit, manufacturing profit, and selling profit; that the average income having its source in North Carolina on the basis of this evidence did not in any event exceed 21.7 percent, and was probably even lower; and that this was out of all proportion to the income apportioned pursuant to formula during the years in question which ranged from 66 to 85 percent.

The Court's language distinguishing its holding from the *Underwood* and *Bass* cases and reiterating the appropriate criteria for evaluating constitutional challenges to the application of State apportionment formulas as applied to net income is most instructive:

> Evidence which was found to be lacking in the *Underwood* and *Bass* cases is present here. . . . In the *Underwood* case,

> it was not decided that the entire net profits of the total business were to be allocated to Connecticut because that was the place of manufacture, or, in the *Bass* case, that the entire net profits were to be allocated to New York because that was the place where sales were made. In both instances, a method of apportionment was involved which, as was said in the *Underwood* case, "for all that appears in the record, reached, and was meant to reach, only the profits earned within the State." The difficulty with the evidence offered in the *Underwood* case was that it failed to establish that the amount of net income with which the corporation was charged in Connecticut under the method adopted was not reasonably attributable to the processes conducted within the borders of that State; and in the *Bass* case the court found a similar defect in proof with respect to the transactions in New York. [283 U. S. at 132-33.]

As was the case in *Underwood* and *Bass*, and in contrast to the showing made in *Hans Rees*, Moorman has made no effort to identify the precise source of its profits, and there is nothing in the record to justify a finding that the apportionment actually made to Iowa was unreasonable. Under such circumstances, as the Court made clear in *Hans Rees*, "in light of the difficulty of making an exact apportionment," an apportionment formula "will be sustained until proof is offered of an unreasonable and arbitrary application in particular cases." 283 U. S. at 133.

Since its decision in the *Hans Rees* case, the Court has on three occasions considered constitutional challenges to the application of a State's apportionment formula to a taxpayer's net income. In each instance the Court has rejected the challenge, and has reaffirmed the basic principles established in *Underwood*, *Bass*, and *Hans Rees*. In *Kent-Coffey Mfg. Co.* v. *Maxwell*, 291 U. S. 642 (1934), *aff'g per curiam* 204 N. C. 365, 168 S. E. 397 (1933), the Court upheld over Due Process Clause and Commerce Clause objections the application of North Carolina's single-factor property formula to the taxpayer's net income. The taxpayer had complained that the apportionment of over 99% of its net income to North Carolina was impermissible in light of

the fact that less than 1% of its sales were made in the State. The Court's affirmance on the ground that the case was controlled by *Underwood* rather than *Hans Rees*, 291 U. S. at 642, was no doubt based on the failure of the taxpayer to show the precise source of its net income—as Moorman here has failed to do—so as to demonstrate the alleged unreasonableness of the formula's application.

In still another case arising out of North Carolina, the Court sustained against constitutional attack the application of a single-factor mileage formula in the calculation of a railroad's net income apportionable to North Carolina, *Norfolk & Western Ry.* v. *North Carolina* ex rel. *Maxwell*, 297 U. S. 682 (1936). Rejecting the usual arguments by the taxpayer of gross overreaching by the State—including a contention supported by evidence that operating costs were higher than average in North Carolina—the Court noted: "For all that appears in the case developed by the Railway, actual gross revenues in North Carolina may have been so far in excess of average gross revenues computed under the statute as to neutralize the discrepancy between actual and average costs of operation." 297 U. S. at 686. Once again the Court emphasized that: "A finding that the statute . . . is oppressive toward the railway in its practical operation cannot rest upon so fragmentary and partial showing of facts. We must bear in mind steadily that the burden is on the taxpayer to make oppression manifest by clear and cogent evidence." *Id.* at 688.

The Court's most recent opinion addressing the constitutional issues raised by a challenge to the application of a net income apportionment formula is *Butler Bros.* v. *McColgan*, 315 U. S. 501 (1942). Following established principles, the Court once again upheld the application of the State's apportionment formula, based on property, payroll, and sales, to the taxpayer's overall net income, over the vehement objection that the operations in the taxing State were actually being conducted at a loss. To this the Court responded with the now familiar refrain: "The

fact of the matter is that appellant has not shown the precise sources of its net income of $1,149,677. If factors which are responsible for that net income are present in other States but not present in California they have not been revealed. At least in absence of that proof, California was justified in assuming that the San Francisco branch contributed its aliquot share to the advantages of centralized management of this unitary enterprise and to the net income earned." 315 U. S. at 509.

Three basic principles thus emerge from this Court opinions that have considered constitutional challenges to the application of state apportionment formulas to a taxpayer's net income. First, it is impossible to identify on an *a priori* basis the precise sources of net income derived from a unitary business engaged in manufacturing and selling—as was Underwood and Bass, and as is Moorman. Second, in light of the first principle, the States are given the utmost leeway both in their choice and application of formulas for apportioning the net income of unitary businesses carried on partly within their borders. Third, a taxpayer challenging the application of such a formula on constitutional grounds bears the heavy burden of demonstrating by clear and cogent evidence the precise sources of its net income to establish that the result achieved through the formula is in fact grossly distorted. In view of these principles, it is apparent that Moorman has not made out a sufficient case for overturning on constitutional grounds, the application of Iowa's single-factor sales formula to its net income.[5]

Moorman, while paying little more than lip service to the decisions discussed above, places its principal reliance instead upon this Court's decision in *General Motors Corp.* v. *District of Columbia*, 380 U. S. 553 (1965). Moorman's reliance is plainly misplaced, as indicated above (see pp. 20-22, *supra*).

5. While the critical defect in Moorman's case is evidentiary, it might also be noted that in four out of five of the cases in which the Court sustained net income apportionments, a single-factor formula was at issue, and in several cases, the allegations of unreasonableness were far more extreme than those made here.

Moreover, in light of the fact that it is only in the application of a formula to the net income of a particular taxpayer that an evaluation of its constitutionality can properly be made, it would be of little moment here even if the Court in the *General Motors* case had struck down the application of the District of Columbia sales factor formula to General Motors on constitutional grounds. For that would no more establish the unconstitutionality of Iowa's sales formula as applied to Moorman than the decision in *Hans Rees*, finding North Carolina's property formula unconstitutional as applied to one taxpayer, determined the result in *Kent-Coffey*, finding constitutional the application of the same formula to another taxpayer. See pp. 30-31, *supra*.

B. The Iowa Formula for Apportioning Net Income to the State Is Constitutional as Applied to Moorman Under the Commerce Clause.

The standards for determining the constitutionality of an apportionment formula's application under the Commerce Clause are substantially the same as those considered in connection with the Due Process Clause. See, *e.g.*, *Norfolk & Western Ry.* v. *State Tax Commission*, *supra;* see, also, pp. 10-11, *supra*. Indeed, as noted above, virtually all the cases discussed in the previous section involved challenges on both Due Process and Commerce Clause grounds and there is nothing in those cases to suggest that the Clauses have different implications in this context. It is, therefore, apparent that what has been said in discussion of Due Process is equally applicable here. To avoid repetition, only those additional matters relating to the Commerce Clause will be addressed here.

First, as suggested earlier, there is serious question whether the Commerce Clause may be relied upon at all as a basis for invalidating the Iowa tax as applied to Moorman. According to the stipulated facts, Moorman's products were manufactured in Illinois and shipped to Moorman's warehouses in Iowa. (App. 24.) Sales in Iowa were made by Iowa salesmen and warehouse-

men from Moorman's Iowa warehouses to Iowa customers. (App. 24.) These are not interstate sales; there is no interstate commerce affected by imposition of this tax. The fact that Moorman is a foreign corporation does not translate the tax into a burden on interstate commerce. The fact that, before the goods came to rest in Iowa warehouses, they made the journey from Illinois, does not make the Iowa sales into sales in interstate commerce. Hence, so far as Moorman is concerned, the tax in question here may be regarded as a tax on intrastate commerce only, with the measure of the tax a proportionate share of its net income.

Even assuming that the Commerce Clause does apply to Moorman's activities, however, it is apparent that Moorman's contentions on this score falter for the same reasons they fail with respect to the Due Process Clause. Moorman again misconceives the operation of the Iowa apportionment formula as applied to its net income. Thus Moorman refers to the amount of its federal taxable income apportionable to Iowa ($1,548,284 or approximately 22% of its apportionable income) as "[t]he total income derived from the manufacture and sale of goods to Iowa customers." (Appellant's Br. 11-12.) But the simple truth is that there is nothing in the record to support that statement because the record does not reveal the precise sources of Moorman's net income on a functional or geographical basis. It reveals only Moorman's overall federally-based net income to which the apportionment formula applies. See page 24, note 3, *supra*. Thus, application of the Iowa formula to Moorman's apportionable federal income does not, as Moorman suggests, determine Moorman's actual "net income resulting from the manufacture and sale of its products to Iowa customers." (Appellant's Br. 11.) Rather, it determines that portion of Moorman's overall net income that is being apportioned to Iowa on the basis of its sales in Iowa; for all that the record shows, the net income Moorman actually derived from its activities in Iowa would have been much higher if the sources of Moorman's net

income could have been precisely identified. It is Moorman's failure to identify these precise sources and to show by clear and cogent evidence that the apportionment made was grossly out of line with the sources so identified which requires that the apportionment be upheld in this case.

Moorman's speculative observations on the possibility of multiple taxation add little to its argument. Indeed, its hypothetical illustrations dramatize its failure to point to any evidence in the record that by taxing some 22% of its apportionable income, Iowa has in fact assigned to itself a disproportionate share of Moorman's profits. Moreover, it is plain that the Court will not strike down as unconstitutional one State's apportionment formula merely because another State's apportionment has been conceived on a different basis. See Point V, *infra*. "Unless a palpably disproportionate result comes from an apportionment, a result that makes it patent that the tax is levied upon interstate commerce . . . this court has not been willing to nullify honest state efforts to make apportionments." *International Harvester Co.* v. *Evatt*, 329 U. S. 416, 422-23 (1947). More recently the Court has pointed out that the constitutionality of one State's statutes cannot depend upon the present configuration of the statutes of another State. *Austin* v. *New Hampshire*, 420 U.S. 656, 668 (1975).

Moorman is likewise in error in suggesting that the mere "risk" of multiple taxation rather than actual proof of multiple taxation is the test for evaluating the constitutionality of an apportionment formula's application under the Commerce Clause. (Appellant's Br. 13.) In *Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U. S. 450, 463 (1959), the Court flatly stated, after noting that "[t]here is nothing to show that multiple taxation is present," that "[w]e cannot deal in abstractions. In this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense." Moorman seeks to find support for its position in such cases as *J. D. Adams Mfg. Co.* v. *Storen*, 304 U. S. 307

(1938), and *Evco* v. *Jones*, 409 U. S. 91 (1972), that refer to the "risk" of multiple taxation as the appropriate criterion. (Appellant's Br. 13.) But Moorman fails to note the critical distinction between the types of taxes involved. In *J. D. Adams* and *Evco* the Court was dealing with unapportioned gross receipts taxes, where the inherent risk of multiple taxation is self-evident. Here, as in *Northwestern*, we are dealing with an apportioned net income tax, where the risk of multiple taxation is small, and to the extent that it does exist, must be demonstrated by the taxpayer under the same exacting standards that are applicable to all constitutional challenges to state apportionment formulas.

Furthermore, Moorman's heavy reliance on *General Motors Corp.* v. *District of Columbia*, *supra*, is as misplaced in the Commerce Clause context as it was in the context of the Due Process Clause. See p. 32, *supra*. This Court's general observations about the possibility of multiple taxation can hardly be regarded as constitutional doctrine in light of its comments regarding the limited scope of its decision. Moreover, nothing in *General Motors* undermines the basic principle that it is only in light of the particular application of an apportionment formula to the net income of a taxpayer that its constitutionality can properly be evaluated. In view of that principle, the *General Motors* dictum can hardly affect the result here, which is required not only by the controlling constitutional standards but also by the insufficiency of Moorman's evidentiary showing.

In short, Moorman has failed to discharge the heavy burden that the guiding constitutional principles impose upon it of demonstrating by clear and cogent evidence that the application of Iowa's apportionment formula produced a grossly distorted result. As Judge McCormick, concurring in the Iowa Supreme Court's decision, succinctly put it:

> In the present case, Moorman did not attempt to prove the amount of its actual net income from Iowa activities in the years involved. Therefore no basis was presented for

> comparison of the corporation's Iowa income and the income apportioned to Iowa under the formula. In this era of sophisticated accounting techniques, it should not be impossible for a unitary corporation to prove its actual income from activities in a particular state. However, Moorman showed only that its tax liability would be substantially less if Iowa employed a three-factor apportionment formula. We have no basis to assume that the three-factor formula produced a result equivalent to the corporation's actual income from Iowa activities. Having failed to establish a basis for comparison of its actual income in Iowa with the income apportioned to Iowa under the single-factor formula, Moorman did not demonstrate that the single-factor formula produced a grossly unfair result. Thus it did not prove unconstitutionality of the formula as applied. [254 N. W. 2d at 757.]

III.

THIS COURT CANNOT INVALIDATE THE APPLICATION OF IOWA'S APPORTIONMENT FORMULA WITHOUT EFFECTIVELY OVERRULING ITS OWN LEADING PRECEDENTS IN THE STATE TAX FIELD AND SERIOUSLY DISRUPTING THE EXISTING FRAMEWORK FOR CONSTITUTIONAL ADJUDICATION IN THIS AREA.

It is appropriate to observe that disposition of this appeal has serious implications for the existing framework of constitutional adjudication in the State tax field far beyond the context of State apportionment formulas. This Court, out of a proper respect for State taxing authority, has rejected Due Process and Commerce Clause objections to exercises of State tax power far more extensive than are even alleged in this case. Thus, in *General Motors Corp.* v. *Washington*, 377 U. S. 436 (1964), and more recently in *Standard Pressed Steel Co.* v. *Department of Revenue*, 419 U. S. 560 (1975), the Court upheld taxes on the unapportioned gross receipts of taxpayers who, like Moorman, manufactured outside the taxing State all their goods sold in the taxing State. In *General Motors*, the State of Washington imposed its tax on the unapportioned gross receipts from GM's sales of motor

vehicles, parts and accessories delivered in the State. All of these articles were manufactured outside the State of Washington. 377 U. S. at 442. In *Standard Pressed Steel*, the State of Washington imposed its tax on the unapportioned gross receipts from Standard's sales of aerospace fasteners to its Washington customers. All of these articles were manufactured outside the State of Washington. 419 U. S. at 561. Indeed, in *Standard Pressed Steel*, the only in-state activities of the taxpayer were the presence of a single in-state employee and the occasional visits of its nonresident engineers—far less than Moorman's extensive activities in the State of Iowa. Yet the Supreme Court dismissed the Due Process objection as "frivolous," 419 U. S. at 562, and had little difficulty disposing of the Commerce Clause claim. *Id.* at 562-63. While one might attempt to distinguish the Washington cases from the instant case on the grounds that the tax there involved a "privilege" tax measured by gross receipts (rather than a net income tax), this Court just last Term made it perfectly clear that such labels had no role to play in the proper analysis of the constitutional limitations on State taxation. *Complete Auto Transit, Inc.* v. *Brady*, 430 U. S. 274 (1977). Thus, the invalidation of the Iowa tax in this case cannot be accomplished without effectively overruling the *General Motors* and *Standard Pressed Steel* cases, and the precedents on which they relied.

Moreover, if, as the Washington cases clearly indicate, the imposition of an unapportioned gross receipts tax on Moorman's sales in Iowa would violate neither the Due Process nor Commerce Clauses, it is difficult to imagine how Iowa's apportioned net income tax, apportioned by those same sales, could do so. For, as this Court has pointed out, the former poses a far greater threat to interstate business than the latter since "tax on gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise . . . and may be sufficient to make the difference between profit and loss," whereas a tax on net income, as is here at issue, "does not arise

at all unless a gain is shown over and above expenses and losses, and . . . cannot be heavy unless the profits are large." *United States Glue Co.* v. *Town of Oak Creek*, 247 U. S. 321 (1918). In short, if this Court were to strike down Iowa's apportioned net income tax in this case, it would *a fortiori* be effectively overruling numerous precedents upholding unapportioned gross receipts taxes on interstate businesses. See, *e.g.*, in addition to Washington cases discussed above, *International Harvester* v. *Department of Treasury*, 322 U. S. 340 (1944); *Allied Mills Inc.* v. *Department of Treasury*, 318 U. S. 740, *aff'g per curiam* 220 Ind. 340, 42 N. E. 2d 34 (1942); *American Manufacturing Co.* v. *St. Louis*, 250 U. S. 459 (1919). The result would be seriously and unjustifiably to disrupt the existing framework for constitutional adjudication in this complex area.

IV.

THE STATUTORY REQUIREMENT THAT NET INCOME BE APPORTIONED TO IOWA BY THE RATIO OF IOWA SALES TO TOTAL SALES IS CONSTITUTIONAL ON ITS FACE AND AS APPLIED TO MOORMAN UNDER THE EQUAL PROTECTION CLAUSE.

As the Iowa Supreme Court recognized, 254 N. W. 2d at 752-54 (App. 134-39), Moorman's objections to the apportionment provisions of the Iowa corporate income tax statute on Equal Protection grounds are insubstantial. Whatever classifications the statute makes (or can be deemed to make) are plainly within the wide bounds of discretion accorded State legislatures under the Equal Protection Clause:

> [The Equal Protection Clause] imposes no iron rule of equality, prohibiting the flexibility and variety that are appropriate to reasonable schemes of state taxation. The State may impose different specific taxes upon different trades and professions and may vary the rate of excise upon various products. It is not required to resort to close distinctions or to maintain a precise, scientific uniformity with reference to composition use or value. . . .

> Similarly, it has long been settled that a classification, though discriminatory, is not arbitrary nor violative of the Equal Protection Clause of the Fourteenth Amendment if any state of facts reasonably can be conceived that would sustain it. . . . [*Allied Stores of Ohio, Inc.* v. *Bowers*, 358 U. S. 522, 526-28 (1959).]

See also *Lehnhausen* v. *Lake Shore Auto Parts Co.*, 410 U. S. 356 (1973).

In light of these principles, it is apparent that Moorman's Equal Protection arguments may be disposed of summarily. For even if the statute were deemed to make a distinction between various types of businesses being carried on in Iowa—or even similar businesses being carried on in different ways—the State legislature may rationally regard such differences as significant and is therefore free to treat them differently under its taxing schemes. If any further support is needed for this conclusion, *Kahn* v. *Shevin*, 416 U. S. 351 (1974), surely provides it. The issue there was whether a Florida tax statute providing an annual $500 property tax exemption for widows without providing any comparable exemption for widowers offended the Equal Protection Clause. The Court was thus faced not merely with a classification made between types of businesses —as in the cases cited above (and arguably in the instant case)—where the Court has always granted the States considerable leeway. Rather, it was faced with the distinction made between individuals on the basis of gender, which the Court has viewed under much stricter standards of equality. See, *e.g.*, *Frontiero* v. *Richardson*, 411 U. S. 677 (1973); *Reed* v. *Reed*, 404 U. S. 71 (1971). Nevertheless, the Court rejected the challenge and upheld the statute relying on *Allied Stores* and *Lehnhausen*, and it reaffirmed the principle that where State taxation is concerned, the States are afforded the utmost freedom in drawing lines which in their judgment produce reasonable systems of taxation. That test is clearly met in this case.

V.

FOR THIS COURT TO HOLD THE IOWA APPORTIONMENT FORMULA UNCONSTITUTIONAL WOULD IN EFFECT IMPOSE A UNIFORM FORMULA UPON THE STATES, THUS IMPROPERLY ARROGATING TO THE COURT A FUNCTION ONLY CONGRESS IS CONSTITUTIONALLY ENTITLED TO PERFORM.

The Commerce Clause is an affirmative grant of power to Congress "[t]o regulate commerce . . . among the several States." U. S. Const., art. I, § 8, cl. 2. There is no question that this power is broad enough to support the enactment by Congress of legislation requiring the States to use a particular apportionment formula in taxing income derived from interstate commerce. It is equally clear, however, that this Court has no such power to act affirmatively in performing its limited constitutional function of construing the restrictions imposed on State tax power by the Commerce Clause. Rather it is confined "to the negative approach resulting from a case-by-case resolution of 'the extremely limited restrictions that the Constitution places upon the states. . . .,' *Wisconsin* v. *J. C. Penney Co.*, 311 U. S. 435 (1940)." *Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U. S. 450, 457 (1959). As Mr. Justice Frankfurter put it in his opinion dissenting from the result:

> At best, this Court can only act negatively; it can determine whether a specific state tax is imposed in violation of the Commerce Clause. Such decisions must necessarily depend on the application of rough and ready legal concepts. We cannot make a detailed inquiry into the incidence of diverse economic burdens in order to determine the extent to which such burdens conflict with the necessities of national economic life. Neither can we devise appropriate standards for dividing up national revenue on the basis of more or less abstract principles of constitutional law, which cannot be responsive to the subtleties of the interrelated economies of Nation and State. [*Id.* at 476 (dissenting opinion).]

If this Court were to strike down the Iowa apportionment formula as unconstitutional, it would in effect be prescribing a uniform formula for all the States in plain violation of these principles. For it is only by assuming that the three-factor formula employed by Illinois is the sole appropriate constitutional method for dividing a taxpayer's net income that Iowa's single-factor formula can be deemed to raise any question of unfairness. It is indisputable that if all jurisdictions apportioned net income the way Iowa does, no enterprise would be heard to complain about multiple burdens, overreaching, or the like. It is only because Iowa has chosen to apportion net income in a manner that differs from that employed by Illinois that the issue of unfair apportionment under the Commerce Clause has been raised. But, unless the Court chooses in effect to endorse the Illinois formula rather than the Iowa formula as the single controlling constitutionally acceptable standard, there is no basis for finding that whatever unfairness may allegedly result from the use of two different formulas is the "fault" of Iowa rather than Illinois, to use Moorman's language. (Appellant's Br. 8.) In short, the assumption that would necessarily underlie any determination by this Court that the Iowa apportionment formula was unconstitutional—*i.e.*, that the Illinois three-factor formula is the sole constitutionally acceptable formula—cannot be made consistently with this Court's limited role under the Constitution in acting "negatively" to determine, on a case-by-case basis, whether a particular State levy has transgressed the "extremely limited restrictions that the Constitution places upon the states." *Wisconsin* v. *J. C. Penney*, 311 U. S. 435, 445 (1940), quoted in *Northwestern States Portland Cement Co.* v. *Minnesota*, 358 U. S. 450, 457 (1959).

The lack of power in this Court to prescribe a uniform apportionment formula for the States does not depend, of course, on whether Congress has itself considered whether to exercise its affirmative power under the Commerce Clause by imposing a uniform standard. Nevertheless, the fact that Congress has on numerous occasions contemplated the possibility of legislating

in this area and has repeatedly chosen not to do so[1] would make any such action by the Court in this area especially inappropriate. In light of Congress' deliberate decision not to impose a uniform apportionment formula upon the States in an area in which it alone has the constitutional power to act affirmatively, any action by this Court effectively imposing such a uniform standard upon the States would be doubly offensive: it would exceed the power confided to it under the Constitution and would do so contrary to the expressed intent of that branch of government to which such matters are in fact confided.

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1. Congressional hearings on proposed legislation were held in 1966, *Hearings on H. R. 11798 Before the Special Subcomm. on State Taxation of Interstate Commerce of the House Comm. on the Judiciary*, 89th Cong. 2d Sess. (1966), and in 1973, *Hearings Before the Subcom. on State Taxation of Interstate Commerce of the Senate Finance Comm.*, 93d Cong., 1st Sess. (1973). Bills were passed by the House in 1968, H. R. 2158, 90th Cong., 2d Sess. (1968), see 111 CONG. REC. 14,432-33 (1968), and in 1969, H. R. 7906, 91st Cong., 1st Sess. (1969), see 115 CONG. REC. 17,323 (1969), only to die in the Senate. And legislation in this area has been introduced in Congress in virtually every session for the last decade. *See* Glasser, *Proposed Solutions to Areas of Conflict in Taxation of Interstate Business*, in 1 33rd ANN. N. Y. U. INST. ON FED. TAXATION 983 (1975); New York State Bar Ass'n Tax Section, Committee on Interstate Taxation, *Proposals for Improvement of Interstate Taxation Bills*, 25 TAX LAWYER 433 (1972); New York State Bar Ass'n Tax Section, Committee on Interstate Taxation, *Supplemental Proposals for Improvement of Interstate Taxation Bills*, 27 TAX LAWYER 213 (1974).

CONCLUSION.

For the reasons spelled out above, the judgment of the Supreme Court of Iowa should be affirmed.

Respectfully submitted,

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